EDITOR'S NOTE

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ovember 14, 1984

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84-801

Title: Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corporation, Debtor, Petitioner
v.
City of New York, et al.
and
Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corporation, Debtor, Petitioner
v.
New Jersey Department of Environmental Protect

Court: United States Court of Appeals for the Third Circuit

Counsel for petitioner: O'Neill,Thomas J., McEnroe,William F.

Counsel for respondent: Koerner,Leonard, Ciarcia,James J., Terrell,A. Dennis, Hermann,Robert

ntry	Date	Note	Proceedings and Orders
1	Nov 14 1984	G	Petition for writ of certiorari filed.
3	Dec 10 1984		Order extending time to file response to petition until January 21, 1985.
4	Dec 19 1984		Brief of respondent New York in opposition filed.
5	Jan 22 1985		Brief of respondent New Jersey Dept.of Env. Protection in opposition filed.
6	Jan 23 1985		DISTRIBUTED. February 15, 1985
7	Feb 19 1985		Petition GRANTED. The case is consolidated with 84-801, and a total of one hour is allotted for oral argument. Justice Powell OUT. **
8	Mar 15 1985	G	Motion of the parties to dispense with printing the joint appendix filed.
9	Mar 25 1985		Motion of the parties to dispense with printing the joint appendix GRANTED. Justice Powell OUT.
10	Apr 5 1985	G	Motion of Thomas H. Jackson for leave to file a brief as amicus curiae filed.
11	Apr 4 1985		Brief of petitioner Thomas O'Neill, etc. filed. VIDED.
12	Apr 4 1985		Brief of petitioner Midlantic National Bank filed.
13	Apr 5 1985		Brief amicus curiae of Pacific Legal Foundation filed. VIDED.
15	Apr 17 1985		Order extending time to file brief of respondent on the merits until June 7, 1985.
16	Apr 22 1985		Motion of Thomas H. Jackson for leave to file a brief as amicus curiae GRANTED.
17	Apr 22 1985	G	Motion of respondents for divided argument filed.
18	May 13 1985		Motion of respondents for divided argument GRANTED.
19	Jun 6 1985		Brief amicus curiae of West Virginia, et al. filed. VIDED.
20	Jun 7 1985		Brief of respondent NJ Dept. of Environmental Protection filed. VIDED.
21	Jun 7 1985		Brief of respondent New York filed. VIDED.
22	Jun 7 1985		Lodging received. To be returned to room 5614,

ntry	Date	Note	Proceedings and Orders
			Department of Justice.
23	Jun 7 1985		Brief amicus curiae of United States filed. VIDED.
24	Jun 12 1985		Record filed.
25	Jun 15 1985	G	Motion of petitioner Midlantic National Bank for divided argument filed.
26	Jun 24 1985		Motion of petitioner Midlantic National Bank for divided argument GRANTED.
27	Jun 7 1985		Brief amicus curiae of California filed. VIDED.
28	Jul 18 1985		SET FOR ARGUMENT, Wednesday, October 16, 1985. This case is consolidated with No. 84-801. (1st case) (1 hour).
29	Aug 7 1985		CIRCULATED.
30	Oct 16 1985		ARGUED.

84-805 (1)

NO.

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK,

Respondents.

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner,

v.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,

Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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Questions Presented

1. Whether the right of a trustee in Bankruptcy pursuant to Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), to abandon property of the estate, which admittedly is burdensome to the estate and of inconsequential value to the state, can be restricted by a state as a result of prepetition conduct of the debtor.

2. Whether the decision of the Court of Appeals is inconsistent with this Court's decision in *NLRB* v *Bildisco and Bildisco,* 104 S. Ct. 1188 (1984), in relying upon an exception to the automatic stay contained in Section 362 of the Bankruptcy Code, 11 U.S.C. Section 362, as a basis for judicially inserting an exception to the right of abandonment into Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a).

3. Whether the decision of the Court of Appeals is inconsistent with this Court's decision in *United States* v. *Security Industrial Bank,* 459 U.S. 70 (1982), in construing the Bankruptcy Code as requiring a trustee in bankruptcy to expend assets of the estate to effect an environmental cleanup of facilities operated by the debtor prior to the filing of the bankruptcy petition, which are of no value to the estate, thereby raising constitutional questions arising out of the "takings clause" of the Fifth Amendment.

4 Whether the decision of the Court of Appeals in denying a trustee in bankruptcy the right to abandon property of the estate pursuant to Section 554(a) of the Bankruptcy Code because of purported prepetition violations of state environmental laws is violative of the Supremacy Clause of the federal constitution.

5. Whether judicial imposition of conditions upon the right of a trustee in bankruptcy to abandon property of the estate pursuant to Section 554(a) of the Bankruptcy Code 11 U.S.C. Section 554(a) will impair bankruptcy policy and frustrate effectuation of the objectives of the federal Bankruptcy Code.

6. Whether "abandonment of property of the estate" by a trustee in bankruptcy pursuant to Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), can constitute a violation of state or federal environmental laws and regulations.

7. Whether a state's claim for reimbursement of expenses for the environmental cleanup of property of the debtor is entitled to priority or administrative expense status in a bankruptcy liquidation.

Parties

The appellants in Third Circuit Case No. 83-5142 ("New York Case") were, the City of New York and the State of New York. Also involved in that case were the State of Pennsylvania, the Department of Environmental Resources for the State of Pennsylvania and the State of New Jersey, as *amici curiae.* The appellant in Third Circuit Case No. 83-5730 ("New Jersey Case") was the State of New Jersey, Department of Enviornmental Protection. Appellees were Thomas J. O'Neill, Trustee, in both cases, and Midlantic National Bank and James V. Frola and Albert VonDohlin in the New Jersey case. (Case No. 83-5730).

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NO.

IN THE

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OCTOBER TERM, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
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THE CITY OF NEW YORK and STATE OF NEW YORK,
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THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corp., Debtor, petitions for a Writ of Certiorari to review two judgments of the United States Court of Appeals for the Third Circuit in the following cases:

> In the Matter of: Quanta Resources, Corp., a corporation of the State of Delaware, Debtor, The City of New York and the State of New York v. Quanta Resources Corp., Debtor, Thomas J. O'Neill, Trustee (Case No. 83-5142); and,
>
> In re Quanta Resources Corp., Debtor, The New Jersey Department of Environmental Protection (Case No. 83-5730).

A single petition for writ of certiorari covering both cases is filed pursuant to Rule 19.4 of the Rules of the Supreme Court of the United States since the two cases involve identical or closely related questions.

Opinions Below

The opinions of the Court of Appeals for Case No. 83-5142 (App. A, *infra*, 1a to 34a)[1] and Case No. 83-5730 (App. B, *infra*, 35a to 40a) are reported at 739 F. 2d 913 and 927 respectively. The Memorandum Opinion of the District Court in *State of New York and the City of New York* v. *Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corp.* (App. G, *infra*, 52a to 60a) and the opinion of the Bankruptcy Court (App. K, *infra*, 69a to 75a) in the case *State of New York and City of New York* v. *Thomas J. O'Neill* are unreported.

[1] Reference herein to the opinions and judgments below will be by citation to the appendix to this Petition for Certiorari filed by Thomas J. O'Neill, Trustee of Quanta Resources Corp.

Jurisdiction

The judgments of the Court of Appeals in Case No. 83-5154 (App. D, *infra*, 45a) and in Case No. 83-5730 (App. E, *infra*, 47a) were entered on July 20, 1984. On August 16, 1984 the Court of Appeals denied rehearing. (App. F, *infra*, 49a). The jurisdiction of this Court is involked under 28 U.S.C. Section 1254(1).

Constitutional Provisions and Statutes Involved

The constitutional provisions involved are the Supremacy Clause of Article VI and the "takings clause" of the Fifth Amendment. The provisions of the Bankruptcy Code involved are Sections 362, 554, and 704, 11 U.S.C. Sections 362, 554 and 704. The case also involves interpretation of 28 U.S.C. Section 959(b). These provisions are printed in the Appendix hereto.

Statement of the Case

These two companion cases, arising out of the same bankruptcy proceeding, present to the Court the question of construction of Section 554 of the Bankruptcy Code, *Abondonment of Property of the Estate*, and the interrelationship of this section with other state and federal laws. The question is presented in the context of the bankruptcy liquidation of a debtor which had engaged in the business of treatment of waste oils, and the attempt by the Trustee to abandon real and personal property of the estate which is alleged to have been contaminated through prepetition conduct of the debtor. The Trustee's abandonment is opposed by the respective environmental agencies of New York and New Jersey who seek to compel the Trustee to clean up the sites.

On October 6, 1981, Quanta Resources Corp. ("Quanta") filed a voluntary petition in bankruptcy under Chapter 11 of the Bankruptcy Code, 11 U.S.C. Section 1101, *et seq.* On November 12, 1981, on motion of the debtor, the proceedings were converted to liquidation under Chapter 7, 11 U.S.C. Section 701, *et seq.* Petitioner, Thomas J. O'Neill, was appointed Trustee on November 18, 1981.

The debtor corporation operated facilities in Edgewater, New Jersey and Long Island City, New York. The New York property was owned by the debtor, while the New Jersey property was leased from two individuals, James Frola and Albert VonDohlin, appellees in the New Jersey Case.

New York

The property is located at 37-80 Review Avenue, Long Island City, New York. Upon his appointment, the Trustee obtained an appraisal report which described the property as follows:

> The subject property has been used for many years as a storage facility for waste oil and is improved with a wide variety of fuel storage tanks. We have been advised that many of these tanks now hold waste oil which is contaminated and effectively, the tanks have little or no market value. Also located on the site are several small concrete block buildings that were used in connection with this operation. In the judgment of the appraiser, the age and condition of these buildings are such that they have no value and should be removed.

The appraiser estimated the fair market value of the propertly as $535,000.00, but stated for "forced sale" purposes he would discount this value by 20% to $428,-

000.00. Mortgages on the property exceeded the "forced sale" value. These appraisal figures did not, however, consider any expenditures which would be necessary in order to dispose of the contaminated oil on the site and render the property marketable.

A considerable quantity of waste oil, sludge and other hazardous wastes, including oil contaminated with PCB's, was stored on the property, and it was estimated that the cost to dispose of the contaminated waste oil properly and otherwise clean up the site would be in excess of a million dollars.[2] While the single fact that the cost to dispose of the waste on the site would exceed the total value of the estate rendered the property valueless, at the onset of the case the Trustee was required to maintain 24 hour guard service because of the property's condition, at a cost in excess of $1,100.00 per week. At the initial hearing before the Bankruptcy Court on the application for abandonment, the Trustee testified that he personally had borrowed $20,000.00 since the inception of the Chapter 7 proceedings, and that much of this money had gone to continue the security. The Trustee simply had no funds whatsoever to pay for continued security, much less to undertake any cleanup operations.

On March 18, 1982, upon request of the Trustee, the Clerk of the Bankruptcy Court issued a notice to creditors of "sale by public auction or abandonment" of the New York property. The notice advised that if the Trustee did not receive an offer in excess of liens on the property, he would abandon the property. No offers were received at the auction sale on April 5, 1982.

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[2] According to New York's Brief before the Third Circuit, following the Trustee's abondonment, the City and State undertook a cleanup operation and expended 2.5 million dollars.

The Trustee subsequently received an offer from Greenpoint Oil Corp. ("Greenpoint"), to purchase the Long Island City property, subject to mortgages and certain other liens for a total price of $3,000.00. This offer was approved by the Bankruptcy Court. Counsel for Greenpoint subsequently advised the Trustee, however, that Greenpoint did not intend to proceed with the purchase because of hazardous conditions and violations existing at the property which Greenpoint was not aware of at the time of the offer. On June 22, 1982, on application of Greenpoint, the Bankruptcy Court voided the approval of the offer.

Although it was the position of the Trustee that, because of the prior notice to creditors the property should then be deemed to have been abandoned as of April 5, 1982, a new notice of proposed abandonment was mailed to all creditors on May 25, 1982. In reponse to the second notice to creditors, the State of New York filed an objection with the Bankruptcy Court on June 4, 1982. On June 7, 1982, the City of New York also filed an objection.

Oral argument on the objections was conducted before the Honorable D. Joseph DeVito, United States Bankruptcy Judge, on June 8, 1982. At that time, the Court directed the filing of additional briefs. On or about June 15, 1982 the State of New York filed a Memorandum in Opposition to Abandonment in which, for the first time, the State requested that the Court order that any money spent by the State or City to dispose of waste be deemed a first lien on the property with priority over any other mortgages and liens.[3] No notice of the application to impose a lien was given to the other lienholders on the property.

[3] As of that date, no money had been expended by the City or State.

Following additional argument on June 22, 1982, the Bankruptcy Court authorized the Trustee to abandon the property. The utter futility of directing the Trustee to undertake a cleanup of the sites was recognized by Judge DeVito. He found that:

> The City and State are in a better position in every respect than either the trustee or debtors' creditors to do what needs to be done to protect the public against the dangers posed by the PCB contaminated facility . . . for this Court to grant the relief requested by the Attorney General would do little else than to put into play an exercise in futility, and would possibly delay the parties who could be chargeable with the cleanup of the property or who have other interests to permit them to move in. That should go forth as quickly as possible and I think this determination will work in that direction.

(App. K, *infra*, 73a to 74a). The claim to entitlement to a lien was rejected by the Court as unauthorized under the Bankruptcy Code. An Order incorporating the terms of the Court's oral decision was entered on July 7, 1982, effective June 22, 1982, *nunc pro tunc*. (App. J, *infra*, 66a to 68a).

Notices of Appeal to the District Court were filed on July 16, 1982. Oral argument was conducted before the Honorable Frederick B. Lacey, United States District Court Judge, on January 24, 1983. At that time, and in a Memorandum Opinion, (App. G, *infra*, 52a to 60a), Judge Lacey affirmed the decision of the Bankruptcy Court. The New York appeal was docketed in the Third Circuit on February 28, 1983.

New Jersey

In addition to the Long Island facility, Quanta operated a waste oil facility located at 1 River Road, Edgewater, New Jersey which consisted of storage and product tanks and equipment for the processing of oil. In June, 1981, a sampling of the waste oil at the site by the New Jersey Department of Environmental Protection ("NJDEP") determined that levels of PCB's were present in the oil in excess of the levels permitted under the temporary operating authorization issued in 1978. On July 2, 1981, Quanta agreed to cease its operations upon NJDEP's request. NJDEP further directed that certain remedial steps be undertaken by Quanta. The filing of the bankruptcy petition intervened.

For the Trustee to implement the remedial measures would have exhausted the entire estate. The Trustee simply did not and does not have resources adequate to maintain and protect the site much less implement remedial actions. Under such circumstances, the Trustee had no alternative but to seek authorization to abandon. Unlike New York, the debtor did not own the New Jersey real estate, and therefore the application for abandonment was limited to the oil in the tanks. An Order was entered by the Bankruptcy Court on May 20, 1983, authorizing the abandonment of the property effective May 17, 1983 *nunc pro tunc*. (App. I, *infra*, 64a to 65a).

Since the identical issue presented in the New Jersey case was already pending before the Court of Appeals, a notice of appeal by agreement to the Court of Appeals under 28 U.S.C. Section 1293(b) was filed on behalf of the New Jersey Department of Environmental Protection on September 21, 1983.

The New York case was argued before the Court of Appeals for the Third Circuit on October 24, 1983. No argument was heard in the New Jersey case. Opinions in both matters were filed July 20, 1984, reversing the decisions of the Bankruptcy and District Courts. The Trustee filed a Petition for Rehearing in both matters, and on August 16, 1984, rehearing was denied. (App. F, *infra*, 49a to 51a).

The Court of Appeals failed to recognize the realities in these cases. The administration of the debtors' estate is virtually completed. All assets other than those abandoned by the Trustee have been liquidated. Distribution was made to secured creditors at the time the assets securing their liens were sold, and administrative expenses incurred by the trustee, including but not limited to salaries and use and occupancy claims, have been paid to the extent funds were available. The Trustee has no money from which to finance any cleanup of either facility or to reimburse the government for its cleanup costs. Moreover, at no time did the trustee ever have sufficient assets to do so.

ARGUMENT

The decision of the Court of Appeals that allows governmental units, acting under state and local laws, to restrict the right of a bankruptcy trustee to abandon property pursuant to 11 U.S.C. Section 554(a) and require the trustee to expend and distribute the assets of the estate in a manner other than required under the Bankruptcy Code should be reviewed by this Court because this is an issue of profound importance to the administration of the federal bankruptcy laws which has not been, but should be, settled by the Supreme Court, and because the Court of Appeals decided a federal question in a way in conflict with applicable decisions of the Supreme Court.

A. The decision of the Court of Appeals is contrary to this Court's rule of construction announced in *NLRB* v. *Bildisco & Bildisco,* 104 S. Ct. 1188 (1984), in judicially inserting an exception into the Bankruptcy Code where no such exception was intended or included by Congress.

As one basis for conditioning the trustee's right to abandon, the Court of Appeals referred to the automatic stay provisions of Section 362 of the Bankruptcy Code, 11 U.S.C. Section 362, which provide that "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power" is not stayed by the filing of a bankruptcy petition. 11 U.S.C. Section 362(b) (4).

In *NLRB* v. *Bildisco & Bildisco,* 104 S. Ct. 1188 (1984), it was argued that collective bargaining agreements were not included within the general scope of Section 365(a) of the Bankruptcy Code, 11 U.S.C. Section 365(a), relating to executory contracts. Relying upon the fact that Section 1167 expressly exempted collective bargaining agreements subject to the Railway Labor Act, but granted no similar exception to agreements subject to the National Labor Relations Act, the Supreme Court stated:

> Obviously, Congress knew how to draft an exclusion for collective bargaining agreements when it wanted to; its failure to do so in this instance indicates that Congress intended that Section 365(a) apply to all collective bargaining agreements covered by the NLRB.

Id. at 1195. Here too it must be assumed that Congress knew how to draft an exclusion for governmental actions when it wanted to do so, such as in the case of exception to the automatic stay pursuant to 11 U.S.C., Section 362(a). The failure of Congress to include such an exception in Section 554(a) indicates Congress' intent that the trustee's right to abandon pursuant to Section 554(a) not be subject to any exception for action by governmental units. As stated by District Court Judge Lacey in his opinion affirming the abandonment of the Long Island City facility, "reliance on Section 362 actually undercuts appellant's argument," (App. G, *infra,* 60a), there being no comparable exception for governmental actions contained in Section 554(a) of the Code.

B. The construction of Section 554(a) of the Bankruptcy Code advanced by the Court of Appeals is inconsistent with the decision of the Supreme Court in *United States* v. *Security Industrial Bank,* 459 U.S. 70 (1982), and is violative of the "takings clause" of the Fifth Amendment.

As pointed out by Judge Gibbons in his dissenting opinion in the Third Circuit, this Court in *United States* v. *Security Industrial Bank, supra,* held that:

> The Bankruptcy Act should not be construed to destroy the interest of creditors when a substantial question arises as to whether the act constitutes a taking of property without just compensation.

(App. A, *infra,* 28a). Quoting from *Security Industrial Bank,* Judge Gibbons stated that the holding was a corollary of the longstanding doctrine that the Court is obligated:

> First (to) ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided . . . similarly, in the absence of a clear expression of Congress intent . . . (a court should) decline to construe the Act in a manner which could in turn call upon the Court to resolve difficult and sensitive questions arising out of the guarantees of the "takings clause". (Citations omitted).

(App. A, *infra,* 28a)

The majority's construction of Section 554(c) of the Bankruptcy Code raises a substantial question under the "takings clause" of the Fifth Amendment, U.S. Const., Amend. 5,[4] since the requested cleanup of the properties

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[4] The dissenting opinion contained the following discussion on this point:

> The "taking" concern has been raised previously:
>
> [T]he public interest cannot demand the erosion of the bankrupt's assets to the point of confiscating practically the entire estate. At some point the extent and degree of taking runs into the constitutional prohibition in the Fifth Amendment [on] the taking of private property for public use without just compensation.

(Footnote continued on following page)

would completely exhaust the assets of the estate, both secured and unsecured. A construction of Section 554(a) of the Code is available, however, which would avoid this difficult constitutional question. Section 554(a) provides that:

> After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

11 U.S.C. Section 554(a). There is no question here but that the two facilities were burdensome to the estate and of inconsequential value to the estate.[5] Having satisfied this criteria, the plain language of Section 554(a) permits abandonment in both cases, thereby avoiding the constitutional question under the "takings clause" of the Fifth Amendment.

(Footnote continued from preceding page)

> In re New York, New Haven and Hartford Railroad Co., 330 F. Supp. 131 147 (D. Conn 197): see also H.R. Rep. No. 595, 95th Cong. 1st Sess. 423 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News, 5963, 6379:
>
> Subsection (a) [11] U.S.C. Section 1170(a) permits the court to authorize the abandonment of a railroad line if the abondonment is consistent with the public interest and either in the best interest of the estate or essential to the formulation of a plan . . . The authority to abandon or not to abandon lines of railroad is, of course, subject to the fifth amendment of the Constitution, which may in particular cases require abandonment in order not to erode a secured creditor's interest in the debtor's property even though the public interest dictates otherwise.

(App. A, *infra* 29a to 30a).

[5] The majority held that "this factual finding is not challenged on appeal." (App. A, *infra* 5a).

Under the holding of *United States* v. *Security Industrial Bank, supra,* the Court must read Section 554(a) in such a manner as to avoid the constitutional question. Accordingly, Section 554(a) must be read as permitting abandonment under the facts of this case. This Court should grant this petition for certiorari in order to insure conformity with the *Security Industrial Bank* decision.

C. 28 U.S.C. Section 959(b) does not constitute a bar to abandonment by the Trustee.

Following a lengthy analysis of the provisions of 28 U.S.C. Section 959(b), the Court of Appeals admitted that Section 959(b) was "not itself an independent prohibition of the trustee's abandoning property in contravention of state law . . .", and that the scope of the section could be construed as limited to administration of the debtor's business as a going concern (App. A, *infra,* 17a). The Court further cited the interpretation of Section 959(b) found in Moore's:

> But Section 959(b) applies *only to the receiver in his operation of the property in his possession.* It does not require the federal receivership court to comply with state laws regulating the distribution of funds in receivership, although Erie R. Co. v. Tompkins should now require it to do so in cases involving only non-federal matters. (emphasis added)

7-pt 2 Moore's Federal Practice, 66.04[4] at 1913 (J. Moore & J. Lucas 2d ed. 1982) (footnotes omitted). Since Section 959(b) is not an independent bar to abandonment, can reasonably be construed as limited in scope to an ongoing business, and since the only cited authorities support this limitation, it is respectfully submitted that 28 U.S.C. Section 959(b) does not prohibit abandonment by the trustee in this case.

D. Abandonment of property of the estate by a Trustee in Bankruptcy in accordance with 11 U.S.C. Section 554(a) does not violate state laws or regulations.

The Court of Appeals made a fundamental mistake in its statement of the issue presented on appeal. The majority opinion in Case No. 83-5142 states the issue as:

> Does 11 U.S.C. Section 554 (1982) permit the abandonment of property of the bankrupt estate in contravention of state and local environmental protection laws?

(App. A, *infra,* 3a). Again in Case No. 83-5730, involving the New Jersey site the court held that:

> The trustee does not have the right to abandon property of the estate where abandonment contraevenes state public health and safety laws, as it does here.

(App. B, *infra,* 39a). In each case, the majority made an assumption, not supported by fact or law, that abandonment by the Trustee would violate state law.

The issue should be stated as whether governmental units, acting under state and local laws, can restrict the right of a trustee to abandon property pursuant to the federal Bankruptcy Code and require that the trustee expend and distribute the assets of the estate in a manner other than that required under the Bankruptcy Code. It is respectfully submitted that this is a question of vital importance in the administration of the Bankruptcy Code which should be settled by this Court.

The history and purpose of abandonment under the prior Bankruptcy Act and the present Bankruptcy Code indicate that the right has evolved from a "judge made rule" to a congressionally recognized power under the Bankruptcy Reform Act of 1978.[6] Discussing the background and legislative history of a trustee's right to abandon property of the estate, Collier states that:

> No provision, however, specifically dealt with the abandonment of burdensome property in liquidation cases. By analogy to the trustee's power to reject executory contracts, cases under prior law permitted the trustee to abandon property that was either worthless or overburdened, or for any other reason when it was certain that the property would not yield any benefit to the general estate. This practice furthered the *paramount purpose of bankruptcy liquidation: the reduction of the debtor's property to money as expeditiously as practicable so as to secure funds for distribution to general creditors. Forcing a trustee to retain and administer property that was valueless or unprofitable is contrary to that purpose.* (emphasis added)

4 Collier on Bankruptcy, Section 554.01 (15th Ed.) Collier goes on to state that:

> Former section 70a of the Act vested title to the debtor's property in the trustee. Abandonment then divested the trustee of this title and revested it in the debtor. Under Section 541, the Trustee no longer takes title to the debtor's property, and, upon abandonment under Section 554, the trustee is simply divested of control of the property because it is no longer part of the estate. Thus, abandonment constitutes a divesture of all interests in the property that were property of the estate.

[6] As such, decisions under the prior Bankruptcy Act relied upon by the Court of Appeals are not persuasive authority. See *Ottenheimer* v. *Whitaker,* 198 F. 2d 289 (4th Cir. 1952), affirming 102 F. Supp. 913 (D. Md. 1952), and *In re Lewis Jones,* 1 B.C.D. 277 (Bk. Ct. E.D. Pa. 1974).

4 Collier on Bankruptcy, Section 554.02 (2) (15th Ed.)

When a trustee abandons property, the property stands as if no bankruptcy had been filed. The property reverts back to the debtor as of the date of the commencement of the proceedings. In effect, the debtor is treated as having owned it continuously. *Mason* v. *CIR,* 646 F. 2d 1309 (9th Cir. 1980). Liens encumbering property abandoned by the trustee are not affected, and the debtor holds in the same manner as prior to the filing of the bankruptcy. *In re Tarpley,* 4 BR 1945 (Bktcy Ct. Tenn. 1980). The Trustee is deemed to have never had title to or custody of the property.

Upon abandonment, the trustee here stands as if he never had an interest in either facility. He has neither taken any action nor refrained from taking any action that would subject him to liability under state or local laws. To suggest that the trustee could be personally exposed to criminal sanctions solely by virtue of his appointment by a federal court to serve as a trustee in bankruptcy is proof of how the objectives of the Bankruptcy Code will be frustrated by the Court of Appeals' decision.

It would be a different matter, of course, if the trustee had actually operated the property in his possession, which post-petition operation resulted in violations of environmental laws. Here, however, the trustee did not operate either facility. To equate the trustee's sole act

of taking custody of the property between the date of his appointment and the date of the abandonment to a disposal of hazardous wastes in violation of federal, state and local environmental laws quite obviously is a strained interpretation of the concept of abandonment. There being no violation of law on the part of the trustee, the trustee cannot be denied the right to abandon assets of the estate based upon these laws. For the trustee not to abandon this property would be violative of his duties enumerated in 11 U.S.C. Section 704. The trustee's duty to abandon unprofitable property is also stressed in *In re Harper,* 175 F. 412 (N.D.N.Y. 1910); *In re Zehner,* 193 F. 787 (A. D. La. 1912); *In re Watts,* 19 F.2d 526 (E.D. La. 1927); and *Bowman* v. *Towery,* 207 Okla. 4, 248 P. 2d 1030 (1952).

E. The decision of the Court of Appeals will frustrate effectuation of the objectives of federal bankruptcy legislation.

How are claims of state and local governmental for environmental cleanup costs to be treated in liquidation proceedings under the Bankruptcy Code? It is respectfully submitted that the decision of the Court of Appeals on this question is contrary to several provisions of the Bankruptcy Code and will effectively render bankruptcy administration in the circumstances of this case impossible.

1. Courts cannot create categories of priorities or administrative expenses not recognized by the Bankruptcy Code.

Courts have consistently held that the original and primary purpose of bankruptcy legislation is the reduction of the debtors' property to money as expeditiously as

practical, and a fair and equitable distribution of the property of the debtor to and among his creditors. States, by means of their own laws, cannot devise preferences among creditors of the debtor which the federal bankruptcy law does not recognize. *In re Universal Money Order Co.,* 470 F. Supp. 869 (S.D. N.Y. 1977); *In re Good Deal Supermarkets, Inc.,* 384 F. Supp. 87 (D. N.J. 1974).

The governmental authorities in these cases are seeking to compel the trustee to retain and administer property which is valueless and unprofitable, and to expend assets, which would otherwise be available for distribution to creditors, to maintain the property and dispose of the hazardous wastes located on the sites. In effect, the states are attempting to obtain a preference of one class of creditors over another, contrary to the express provisions and purposes of the Bankruptcy Code. Under such circumstances, the Supremacy Clause of Article VI of the Constitution demands that the conflict between the Bankruptcy Code and state legislation be resolved in favor of the Bankruptcy Code. Abandonment must be permitted.

Although the Court of Appeals recognized that "state law regulating the distribution of assets among creditors must give way to the all encompassing law of creditors' rights", (App. A, *infra,* 18a) the Court failed to recognize that, in effect, the denial of the trustee's right to abandon will result in a distribution of assets among creditors pursuant to state law rather than federal law. This result clearly is wrong, and frustrates the full effectuation of the objectives of federal bankruptcy legislation.

For the Court to say that the trustee must finance the cleanup would require a rearrangement of the priority of distribution not envisioned by the Bankruptcy Code. Secured and unsecured creditors would be required to pay for the cleanup of the facilities. The result would be to

transfer the cost to parties who were in no way responsible for placing the contaminated oil on the sites. If the Court insists that the cost of cleanup be borne by the innocent, then it is the innocent public who should carry that burden not a select innocent few. As noted by Judge Gibbons, one result is:

> Transferring the cost of cleanup to secured and unsecured creditors of the debtor, in this instance outside New York, who have no interest whatever in the Long Island City property, and who, on the record before us, were in no way responsible for placing the contaminated oil on that site.

(App. A, *infra,* 29a).

The question of the right of governmental units to priority or administrative expense status was addressed by Congress in connection with the enactment of the exception to the automatic stay provisions. 11 U.S.C. Section 362. The Congressional House Report Comments on Section 362 include the following:

> Paragraph (4) excepts commencement or continuation of actions and proceedings by governmental units to enforce police or regulatory powers. Thus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay.

> Paragraph (5) makes clear that the exception extends to permit an injunction and enforcement of an injunction, and to permit the entry of a money judgment, but *does not extend to permit enforcement of a money judgment.* Since the assets of the debtor are in the possession and control of the bankruptcy court and since they constitute a fund out of which all creditors are entitled to share, *enforcement by a governmental unit of a money judgment would give it preferential treatment to the detriment of all other creditors.*

H.R. Rep. No. 595, 95th Cong. First Sess. 343 (1977), reprinted, in (1978), U.S. Code Cong. & Ad. News 5963, 6299. The intent to deny priority or preferential treatment is clear.

As pointed out in the decision in *In re Charles George Land Reclamation Trust,* 30 B.R. 918 (Bkrptcy Ct. D. Ma. 1983), Congress had an additional opportunity to consider the question of the priority of federal and state governmental claims for cost of cleaning up hazardous substances. A bill introduced by Rep. Florio on September 23, 1982 (H.R. 1972) would have given priority to such claims. The bill was defeated. The fact that it was necessary to introduce such a bill also indicates that such priority is not accorded to these claims under the present bankruptcy code.

Upon the failure of a landowner to implement cleanup measurers, both the New York and the New Jersey Statutes relied upon by respondents below are similar in result. If the state undertakes cleanup of the property and disposes of the hazardous waste, the state then becomes entitled to a lien.[7] By way of example, the New

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[7] The City of New York filed a Proof of Claim on October 7, 1982, in the sum of "approximately $5,000,000.00". The City claimed a lien pursuant to New York City Administrative Code Section 564.245 upon the Long Island City premises "for all expenses incurred by the City of New York in securing, removing and properly disposing the materials unlawfully placed there by the debtor."

(Footnote continued on following page)

Jersey Spill Compensation and Control Act, N.J.S.A. 58:10-23.11, *et seq.* creates:

> A first priority claim and lien paramount to all other claims and liens upon the revenues and all real and personal property of the discharger, whether or not the discharger is insolvent."

N.J.S.A. 58:10-23.11f. The claim and liens arise upon any expenditure by the administrator of the New Jersey Spill Compensation Fund.

In this case, the City and State of New York, upon abandonment by the Trustee, received exactly what they claim they are entitled to, a lien on the New York property of the debtor. New Jersey, not yet having made any expenditures, is not entitled to a lien. If and when New Jersey does expend money, it will be free to pursue its remedies against the real property in Edgewater, New Jersey. Since no expenditures were made by any governmental units prior to the filing of the bankruptcy petition, the asserted liens were not perfected or enforceable on the date of the filing, and are therefore avoidable by the Trustee. 11 U.S.C. Section 545.

(Footnote continued from preceding page)

The New York State Department of Environmental Conservation filed a Proof of Claim on July 14, 1982 in an amount "to be determined". The claim states that the cost of removal and disposal of waste oil and other hazardous substances constitutes its claim. New York State also claimed a first lien on the Long Island City property.

The proof of Claim of the New Jersey Department of Environmental Protection, filed July 20, 1982, asserts that it is a "claim for an administrative expense of the estate which should be given priority over all secured claims of the estate". New Jersey further claimed "that all money received by the Trustee from the sale of oil or equipment at the facility in Edgewater should be applied toward the proper closure and cleanup of the facility".

New York and New Jersey further appear to seek a "super-priority" status for their claims such as that contemplated by 11 U.S.C. Section 364(c). Nowhere in the Bankruptcy Code can there be found an express or implied intent to accord such status to any claims other than those expressly set forth in the Code.

As to whether the claims of New York and New Jersey could be accorded administrative expense status under 11 U.S.C. Section 503(b)(1)(A), Judge Gibbons, in his dissenting opinion, characterized as "preposterous" the contention that the cleanup costs for assets which are of no value to the estate could be classified as "necessary costs and expenses of preserving the estate." 11 U.S.C. Section 503(b)(1)(A). While, as noted by the majority, the categories enumerated in Section 503 are not exclusive, it is clear that all categories relate to preservation of the estate. In no way will a cleanup of the properties benefit or preserve the estate. The only result can be the exhaustion of all assets of the estate, and the denial to all other creditors of the right to share in the distribution of the estate.

2. *There exists no basis for subordination of administrative, secured, and other unsecured claims to the claims of New York and New Jersey.*

What the state and local governmental units effectively seek here is a subordination of all other claims, whether secured, super-priority, administrative or unsecured, to their claims. New York seeks reimbursement of the $2.5 million it expended subsequent to the trustee's abandonment of the Long Island City site. New Jersey, not having spent any money, seeks to compel the Trustee to undertake removal of hazardous materials from the Edgewater, New Jersey site. In any event, the states want these claims

to be paid first. New York in seeking to reach assets of the debtor located in New Jersey, actually seeks more than its own statute permits.

Under Section 510 of the Bankruptcy Court, 11 U.S.C. Section 510, courts have jurisdiction to subordinate, on equitable grounds, all or any part of an allowed claim or interest to all or any part of another allowed claim or interest. The Code provides:

> Section 510. Subordination
>
> . . .
>
> (c) Notwithstanding subsection (a) and (b) of this section, after notice and a hearing, the court may—
>
> (1) under priniciples of equitable subordination, subordinate for purposes of distribution all or part of an allowed claim to all or part of another allowed claim or all or part of an allowed interest to all or part of another allowed interest; . . .

Before the Bankruptcy Court will exercise its power of equitable subordination, however, three conditions must be satisfied:

(1) The claimant must have been engaged in some type of inequitable conduct;

(2) The misconduct must have resulted in injury to creditors of the bankrupt or conferred an unfair advantage on the claimant, and

(3) Equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act.

Matter of Mobil Steel Company, 563 F. 2d 692, 700 (5th Cir. 1977); *In re American Lumber Company*, 5 B.R. 470 (D.C. Minn. 1980). The fundamental aim of subordination

is to undo or to offset any inequity in the claim position of a creditor that will produce injustice or unfairness to other creditors in terms of the bankruptcy result. *In re Kansas City Journal-Post Co.*, 144 F. 2d 791 (8th Cir. 1944); *In re Westgate-California Corp.*, 642 F. 2d 1174 (9th Cir. 1981). Generally, the claim will not be subordinated unless it is shown that the claimant has acted inequitably in the course of his relationship with the debtor and that those activities have harmed the debtor or his other creditors in some way. *In re Ahlswede*, 516 F. 2d 784, 788 (9th Cir. 1971); *In re Westgate-California, supra.*

Included in the legislative history to Section 510 is the following:

> It is intended that the term "principles of equitable subordination" follow existing case law and leave to the courts development of this principle. To date, under existing law, a claim is generally subordinated only if holder of such claim is guilty of inequitable conduct, or the claim itself is of a status susceptible to subordination, such as a penalty or a claim for damages arising from the purchase or sale of a security of the debtor. The fact that such a claim may be secured is of no consequence to the issue of subordination. However, it is inconceivable that the status of a claim as a secured claim could ever be grounds for justifying equitable subordination. 124 Cong. Rec. H 11,095 (Sept. 28, 1978); S 17,412 (Oct. 6, 1978).

There is no basis for the subordination sought by respondents. There has been no allegation, and there exists no basis for any allegation, that the Trustee or any other creditor engaged in any inequitable conduct or misconduct which harmed the debtor or respondents. There is no basis in the Bankruptcy Code or case law for subordination of any claims of New York and New Jersey.

3. *Under the circumstances of this case, a Trustee in Bankruptcy has no alternative but to refuse appointment or, once having accepted appointment, to resign.*

Where is a trustee in bankruptcy left under the decision of the Court of Appeals? Does he remain the owner of the property forever? Which site must be cleaned first—New York or New Jersey? Can he be subject to criminal sanctions or personal liability for costs of cleanup? Can the estate never be closed? Can creditors be charged with the cost of cleanup? These and many other important questions are left unanswered.

A good example of the frustration of the purposes of federal bankruptcy law which will result is found in the case of *In re Charles George Land Reclamation Trust,* 30 B.R. 918 (Bkrtcy. D.Ma. 1983). The debtor in that case owned and operated a waste disposal facility. Prior to the filing of a bankruptcy petition, the debtor had entered into a consent judgment with the Commonwealth of Massachusetts requiring the debtor to undertake certain actions to bring the facility into compliance with environmental laws and regulations. The required remedial actions had not been completed as of the filing of the bankruptcy petition. The Commonwealth of Massachusetts argued before the Bankruptcy Court that any trustee would have to immediately rectify the violations of law or otherwise find himself in violation of 28 U.S.C. Section 959(b). As a result, no private panel member would agree to serve as trustee. The United States Trustee, as a default trustee under 11 U.S.C. Section 15701(b), then brought an emergency motion for dismissal. This motion was granted. The present uncertain status of the law in this area, which resulted in the refusal of anyone to serve as trustee, was the reason.

To allow the decision of the Court of Appeals to stand would effectively preclude orderly liquidation of any debtor's estate where the debtor was under an obligation at the time of filing bankruptcy proceedings to take any remedial action under any other federal or state legislation. Nowhere in the Bankruptcy Code can there be found a legislative intent to deny such debtors the rights and protections under the Bankruptcy Code. Quite to the contrary, the Code evidences a congressional intent that claims of governmental units for environmental cleanup not be accorded priority or administrative expense status, but rather share with all other creditors in the distribution of the estate.

F. This court should grant certiorari.

We believe that there are special and important reasons for this Court to grant review on writ of certiorari. We have attempted to illustrate as concisely as possible how extensively the decision of the Court of Appeals will frustrate the objectives of bankruptcy. The uncertainty in bankruptcy law today due to the absence of a definitive answer on this issue from the Supreme Court has made administration of estates of debtors involved in any way with hazardous materials at the very least difficult and dangerous for trustees, if not impossible. The complete reordering of priorities which can result from the decision of the Court of Appeals should be reviewed and settled by this Court. This Court should also review the decisions in light of the apparent inconsistencies with applicable decisions of the Supreme Court.

CONCLUSION

Based upon the foregoing it is respectfully submitted that this Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit be granted.

Respectfully submitted,

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Dated: November 14, 1984

APPENDIX A

Opinion of the United States Court of Appeals for the Third Circuit (No. 83-5142)

No. 83-5142

In the Matter of:
QUANTA RESOURCES CORP.,
a corporation of the State of Delaware

Debtor

THE CITY OF NEW YORK and
THE STATE OF NEW YORK

v.

QUANTA RESOURCES CORP.,
a corporation of the State of Delaware

State of New York
and City of New York

Appellants

On Appeal from the United States
District Court for the
District of New Jersey
(Civil Action No. 82-3524)

Argued October 24, 1983

Before: GIBBONS, GARTH, and
HIGGINBOTHAM, *Circuit Judges*

(Opinion Filed July 20, 1984)

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OPINION OF THE COURT

GARTH, *Circuit Judge*:

This case presents an issue of major importance under the Bankruptcy Reform Act of 1978: does 11 U.S.C. § 554 (1982) permit the abandonment of property of the bankrupt estate in contravention of state and local environmental protection laws? In proceedings before the bankruptcy court, the trustee in bankruptcy here asserted the power to abandon a waste oil processing and storage facility. He was opposed by the State and City of New York, who argued that the trustee's power was limited by state and local laws regulating the abandonment of hazardous wastes. The bankruptcy court granted permission to abandon. The district court affirmed the bankruptcy court. We reverse.

I

Quanta Resources Corp. (Quanta), which owned and operated a waste oil storage and processing facility in Long Island City, New York (the geographic center of New York City), filed a voluntary petition in bankruptcy under Chapter 11 of the Act on October 6, 1981. The action was converted to a liquidation proceeding under Chapter 7 on November 12, 1981. Thomas J. O'Neill (Trustee), the appellee here, was appointed trustee in bankruptcy on November 18, 1981.

The Trustee filed a notice of intention to abandon

the facility under 11 U.S.C. § 554. That section provides that "[a]fter notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate, or that is of inconsequential value to the estate." At the time of the notice there were on the site fuel storage tanks containing more than 500,000 gallons of waste oil and other chemicals, of which at least 70,000 gallons were contaminated with polychlorinated biphenyls (PCB's).

PCB's are extremely hazardous chemicals.[1] Reflecting the hazards associated with these compounds, numerous federal, state, and local laws govern the storage and disposal of PCB's. *E.g.*, 15 U.S.C. § 2605(e) (1982); 40 C.F.R. §§ 761.1-761.80 (1983); N.Y. Envtl. Conserv. Law §§ 27-0900 to 27-0923 (McKinney Supp. 1982); N.Y. Admin. Code Tit. 6, § 366.4(e) (1982); New York, N.Y. Admin. Code § C19-50.0. Compliance with these laws would have required substantial expenditures to guard, repair, and clean up the facility and to dispose of the waste.[2] The Trustee's notice of intention to abandon was predicated on the assertions that the requisite expenditures would render the property a burden on

1. PCB's are themselves toxic. *See generally* Nat'l. Rsch. Council Comm'ee on the Assessment of Polychlorinated Biphenyls in the Environment, Polychlorinated Biphenyls (1979). Their oxidation products (produced upon burning PCB's) are also toxic. Among the oxidation products of PCB's are polychlorinated dibenzo-p-dioxins (the so-called "dioxins") and polychlorinated dibenzo forans, which are powerful carcinogens, teratogens, and liver toxins. Affidavit of Dan Levy, New York State Department of Law Environmental Scientist, App. 19 - 22.

2. At the time of the hearing, Quanta was evidently in violation of a consent order requiring it to bring the facility into compliance with state law. *See* Transcript of Bankruptcy Proceedings, June 8, 1982, at 25.

the estate, and that the property would be of inconsequential or no value to the estate.

At the time of proposed abandonment, the site was subject to two mortgage liens.[3] Although there were objections filed to abandonment, there was no dispute as to the fact that the requisite expenditures would rapidly dissipate whatever equity there was in the property. Thus, the bankruptcy court found that the property was burdensome and of inconsequential or no value to the estate.[4]

The objections to abandonment filed by New York asserted that abandonment of the property would itself violate state and local law. This is because "abandonment" under Section 554 revests title subject to liens in Quanta,[5] which has no other assets, having lost title to these in favor of the estate upon commencement of the bankruptcy case. 11 U.S.C. §541 (1982). Quanta was itself, then, unable to act

3. On March 18, 1982, the Trustee had filed a notice of intended "sale by public auction as abandonment" of the site. The notice stated that if the Trustee did not receive an offer in excess of a lien of the Equitable Life Assurance Society, the property would be abandoned. Objection to the sale was filed by Portland Holding Corp. based on an asserted mortgage lien; the bankruptcy court entered judgment establishing the validity of that lien. An offer to purchase the property subject to the liens was approved by the court, but was subsequently withdrawn on the ground that there were hazardous wastes stored there in violation of law, and that this had not been made known to the purchaser. *See* Transcript of Bankruptcy Court Proceedings, June 8, 1982, at 12. These liens were later abandoned. *See* Affidavit of Nancy Stearns, annex; Affidavit of Carol Moore, Exh. B.

4. This factual finding is not challenged on appeal.

5. Abandonment is to any person with a possessory interest in the property, including the debtor, *See* S. Rep. No. 989, 95th Cong., 2d Sess. 93 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 5879.

with respect to the site. Thus abandonment would, in effect, constitute disposal of the hazardous wastes, *see* N.Y. Envtl. Conserv. Law § 71-7702 (McKinney Supp. 1982) ("disposal"). In addition, abandonment of the facility in its then state of disrepair, itself irremediable by Quanta, would create a continuing violation of state and local hazardous waste storage laws, *see supra*.

New York asserted, therefore, that because these laws are designed to decrease the risk of uncontrolled toxic chemical discharge, abandonment would create a substantial danger to the public health and safety. Thus New York requested that permission to abandon be denied until all hazardous wastes were removed from the property and lawfully disposed of. New York grounded its objection in both "public policy considerations" reflected in the applicable local laws and the provisions of 28 U.S.C. § 959(b) (1982), which requires that a trustee "manage and operate its property in his possession as such trustee. . . according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof."

After a hearing, the bankruptcy court rejected New York's objections and issued an order, on July 7, 1982, permitting abandonment. The court refused to stay the order pending appeal, and refused to grant New York a first lien on the property to the extent of any monies that New York might expend to bring the abandoned property into compliance with law. In fact, following the abandonment New York did proceed to clean up the facility,[6] with the exception of contaminated subsoil, at a cost of about $2.5 million (Affidavit of Richard Mendes).

6. *See* N.Y. Envtl. Conserv. Law § 27-0916 (McKinney Supp. 1982).

New York appealed to the district court from the bankruptcy court's order, without raising the question of New York's right to a first lien. The district court affirmed on January 24, 1983. New York appealed to this court. The Commonwealth of Pennsylvania and the State of New Jersey submitted briefs as *amici curiae*. The questions raised by New York in this appeal are the propriety vel non of abandonment, and New York's right to reimbursement for its cleanup costs as an administrative expense, *see* 11 U.S.C. §§ 503(b), 507(a).

II.

Where it is contended, as it is here, that federal law confers a power that is not limitable by state law, the supremacy clause, U.S. Const. Art. VI, cl. 2, requires that we determine whether application of the state law frustrates the full effectuation of the objectives of federal bankruptcy legislation. *Perez v. Campbell*, 402 U.S. 637, 652 (1971). In general, preemption of state law "is not favored 'in the absence of persuasive reasons -- either that the nature of the regulated subject matter permits no other conclusion, or that Congress has unmistakably so ordained.'" *Consolidated Edison v. Montana*, 453 U.S. 609, 634 (1981) (quoting *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142 (1963)); *see Penn Terra Ltd. v. Department of Envtl. Resources*, No. 83-5448, slip op. at 11 (3d Cir. April 30, 1984). *See also Stellwagen v. Clum*, 245 U.S. 605, 613 (1918) (state laws are suspended only to the extent of actual conflict with the scheme of federal regulation). Thus, analysis must proceed in two stages: first, an examination of the primary purposes of each of the laws at issue; second, a determination whether state law is an obstacle to the effectuation of federal objectives. *Perez*, *supra*, 402 U.S. at 644, 649.

The objectives of federal bankruptcy law can be broadly stated: to provide for an equitable settling of creditors' accounts by usurping from the debtor his power to control the distribution of his assets.[7] *See Kothe v. R.C. Taylor Trust*, 280 U.S. 224, 226 (1930). The purpose of a liquidation proceeding under Chapter 7, as under Chapter VII of the Bankruptcy Code, *see* S. Rep. No. 989, 95th Cong. 2d Sess. 6, reprinted in 1978 U.S. Code Cong & Ad. News 5792 (new law essentially tracks previous law), is to provide a fair distribution of the debtor's assets among the creditors; to that end, a trustee for the creditors is appointed by the court or elected by the creditors. 11 U.S.C. §§ 702 (election), 703 (appointment), 704 (duties). The trustee must collect the debtor's assets for the estate, reduce the assets to money, and distribute the property of the estate. *Id.* §§ 704, 726. The abandonment power embodied in Section 554 enables the trustee to rid the estate of burdensome or worthless assets, and so speeds the administration of the estate, *see id.* § 704(1), and also protects the estate from diminution. In such manner, abandonment serves the creditors' interest in expeditiously obtaining a fair amount on settlement of their claims.

The primary purpose of the state and local laws regulating disposal of hazardous wastes is obviously to protect the public from the toxic effect of dangerous

7. While it has been held that the old bankruptcy law advanced a second purpose, to provide a fresh start for the debtor, *e.g.*, *Kokoszka v. Belford*, 417 U.S. 642, 645-46 (1974) (citing *Berlingham v. Crouse*, 228 U.S. 459, 473 (1913)), that purpose can no longer be said to be advanced in present liquidation law, with respect to nonindividuals (*i.e.*, corporations and partnerships), since the 1978 Act eliminated the provision for discharge of debts of nonindividuals. 11 U.S.C. § 727(a)(1); *see* S. Rep. No. 989, 95th Cong. 2d Sess. 98 (1978), reprinted in 1978 U.S. Code Cong. & Ad. News 5884.

substances by preventing their uncontrolled discharge into the environment.

On the surface, these two purposes cannot be reconciled where the trustee legitimately invokes his power to abandon an asset whose manner of abandonment the state regulates. The question thus presents itself: did Congress intend that the trustee's abandonment power be unrestricted by public health and safety regulations? Our examination of the bankruptcy laws and the authorities interpreting these laws reveals no such congressional intent.

A.

We start with the basic assumption that Congress did not intend to displace state law. *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981); *Penn Terra*, *supra*, slip op. at 11. Where it is argued that Congress intended to withdraw police power from a state, that intention must be unmistakable. *Penn Terra, supra*, slip op. at 11-12.

There is no legislative history of Section 554. Although there had been no express recognition of an abandonment power in the pre-1978 bankruptcy statute, courts approved the trustee's exercise of such a power as part of his larger power to dispose of the assets of the estate. *See* 4A Collier on Bankruptcy ¶70.42 at 502-504 & n. 4 (J. W. Moore 14th ed. 1978) (citing cases); *see also* 11 U.S.C. §§ 64a(4), 70a(2), 70b (1976) (repealed 1978) (provisions contemplating abandonment, respectively, of property against which taxes are assessed; of rights in pending applications for patents, copyrights, and trademarks; and of executory contracts). Section 554 obviously codifies this judge-made law.

Cases under prior law held that "the trustee in the exercise of the power to abandon is subject to the application of general regulations of a police nature."

4A Collier on Bankruptcy (14th ed.), *supra*, ¶ 70.42[2] at 502-04. *Ottenheimer v. Whitaker*, 198 F.2d 289 (4th Cir.), *aff'g* 102 F. Supp. 913 (D. Md. 1952), held that the trustee could not abandon four worthless barges in a harbor, where abandonment would violate federal law relating to the obstruction of the harbor, even though the cost of complying with the laws would be much greater than the value of the barges. The court acknowledged the general rule that the trustee may abandon burdensome property, and then held it inapplicable.

> This rule would be applicable here were it not for the unusual consequences that would follow. There can be no doubt that the property not only has no value, but also that the care and disposition of it will involve the expenditure of a substantial sum of money. But it is equally true that if the trustee abandons the barges and at the same time holds on to the valuable assets of the estate, the title to the barges will revert to the bankrupt and he will be left without means to care for or dispose of them in the manner prescribed by the statute.
>
> In that event, the barges would sink and become an obstruction to the passage of other vessels, and it might well be held that the bankrupt or the trustee had become liable to the punishment of fine or imprisonment prescribed by the statute for the person who voluntarily or carelessly allows a vessel to be sunk in a navigable channel. It seems obvious to us that a rule which is not provided by statute but built up by the courts to facilitate the administration and distribution of the assets of a bankrupt estate should not be extended so as to reach such an unreasonable and unjust result. The judge-made rule must give way when it comes into conflict with a statute enacted in order to

> ensure the safety of navigation; for we are not dealing with a burden imposed upon the bankrupt or his property by contract, but a duty and a burden imposed upon an owner of vessels by an Act of Congress in the public interest.

198 F.2d at 290.

The concerns underlying this decision are, first, the comparative strengths of judge-made law relative to a conflicting statute, and second, the comparative strengths of policies which avoid burdens to the estate relative to the policies respecting safety of the public. With respect to each concern, the court held that the determinations of the legislature and the policy of safeguarding the public were paramount.

Another case, which relied in part on *Ottenheimer* and which emphasized a combination of these two concerns, is *In re Lewis Jones, Inc.*, 1 Bankr. Ct. Dec. 277 (Bankr. E.D. Pa. 1974). The court there held that the trustee could not abandon underground steam pipes, vents, and manholes, where abandonment would infringe on the public interest by creating health and safety hazards. *Lewis Jones* cited the principle announced in *S.E.C. v. United States Realty & Improvement Co.*, 310 U.S. 434, 455 (1940):

> [A] bankruptcy court is a court of equity and is guided by equitable doctrines and principles except as they are inconsistent with the Act. A court of equity may in its discretion, in the exercise of the jurisdiction committed to it, grant or deny relief upon performance of a condition which will safeguard the public interest.

(citations omitted). The trustees in *Lewis Jones* estimated the cost of alleviating the problems to be at least $82,000 (plus $500 per vent to fill in each of an unknown number of vents); there were funds of $328,000 on hand; creditors' claims amounted to

$4,478,000. The court found that the cost was "not too high a price to pay in the public interest." The court then ordered that permission to abandon be conditioned on the trustees' expending funds to fill in and seal the steam openings.

In a case relying similarly on the court's equitable powers, but grounding these in the jurisdiction conferred by statute, the court held that the trustees (in reorganization) for a railroad could not abandon service on a branch line even though operating the line would burden the estate with expenditures. *In re Chicago Rapid Transit Co.*, 129 F.2d 1 (7th Cir.), *cert. denied*, 317 U.S. 683 (1942). In this case the railroad was a public utility, subject to state regulations that limited its power to abandon service without consent of the state authorities. The court first noted that under the supremacy clause, U. S. Const. Art. 6, cl. 2, the sole federal jurisdiction in bankruptcy, "when given expression in legislation by Congress," supersedes all inconsistent state laws. *Id.* at 4. It then observed that the power to abandon burdensome assets was incidental to the powers lodged in the bankruptcy court by the statute, and that "the intent and purport of all bankruptcy legislation, so far as the power to protect the estate is concerned, is largely declaratory of certain recognized equitable principles, namely: the power of a court of equity to protect property in its custody." 129 F.2d at 5. But, the court reasoned, if the traditional authority of the state to regulate local transportation should "be deemed withdrawn by Congress in bankruptcy legislation, evidence of that withdrawal in fit language should be found within the act." *Id.*, citing *Palmer v. Massachusetts*, 308 U.S. 79 (1939). It then held that Congress had not withdrawn the state's authority, and thus the trustees must comply with the valid state laws. The court distinguished the bankruptcy court's power to cancel

burdensome leases, so that the trustees were permitted to cancel the lease of the line from the interstate authority, and were ordered to continue operating the railroad but for the account of the lessor.

By contrast, recently another court held, while citing *Chicago Transit*, that the trustee for a bankrupt hospital could not be prevented from abandoning medical records even though a state law required insolvent hospitals to maintain and store them. *In re Adelphi Hospital Corp.*, Bankr. L. Rep. (CCH) ¶66,882 at 76,856 (2d Cir. 1978) (per curiam). The *Adelphi* court relied on the supremacy clause, and stated simply:

> It is beyond peradventure that federal law prevails over inconsistent state laws. U.S. Const. art. VI, cl. 2; *Gibbons v. Ogden*, 22 U.S. (S Wheat.) 1 (1824). This fundamental principle of American jurisprudence of course encompasses the bankruptcy laws. U.S. Const. art I. §8, cl. 4; *see, e.g., International Shoe Co. v. Pinkus*, 278 U.S. 261, 263-65 (1929). And under federal law, abandonment in this case is clearly permissible. *See In re Chicago Rapid Transit Co.*, 129 F.2d 1, 4-5 (7th Cir.), *cert. denied*, 317 U.S. 683 (1942).
>
> The paramount purpose of bankruptcy liquidation and administration is the reduction of a bankrupt's property to money as expeditiously as practicable, so as to secure funds for distribution to general creditors. Hence the trustee in examining the various assets with regard to their potential value when converted into money for distribution to creditors is from the outset faced with the managerial duty to concentrate on property of possible benefit to the estate and to eliminate property that will be either valueless or unprofitable in its administration. . . The trustee

> . . . may abandon any property which is either worthless, or overburdened, or for any other reason certain not to yield any benefit to the general estate. 4A *Collier on Bankruptcy* ¶ 70.42, at 502 (14th ed. 1976) (footnotes omitted).

Id. at 76,857 (footnotes omitted). The court's bare citation of *Chicago Transit*, which had reached an opposite conclusion, is not very helpful. But the passage it cites emphasizes that the state regulation at issue was a part of public utility regulation of a service operated for public convenience and necessity. Thus *Adelphi* may be read as distinguishing state regulations on the basis of their relative importance to the public of their intrusiveness in the regulation of the industry.

Ottenheimer and *Chicago Transit* have similar rationales, but *Ottenheimer*'s stress in the judge-made character of the power to abandon is lacking in *Chicago Transit*. The two are consistent, however, in their reluctance to override state statutes in the absence of explicit Congressional direction: *Ottenheimer*'s stress on the judge-made character of the power to abandon is comparable to *Chicago Transit*'s emphasis on the lack of explicit intent to override state utility regulations. A common concern may thus be found in all four noted cases: that where important state law or general equitable principles protect some public interest, they should not be overridden by federal legislation unless they are inconsistent with explicit congressional intent such that the supremacy clause mandates their supersession by the abandonment power.

B.

Thus, whether the trustee's power to abandon is limited depends in part on whether there is express federal law that either grants superseding power or

subjugates the abandonment power to state law even if that law would otherwise be inconsistent. Section 554 itself refers only to the trustee's affirmative power to abandon. Considered in the light of other provisions that both limit the supersession of state laws and specifically incorporate equitable principles into a bankruptcy court's jurisdiction, it is clear that Section 554 does not of itself preempt state police power regulations.

That Congress did not intend the bankruptcy scheme generally to abrogate the enforcement of state police power regulations is evidenced by, first, the express exception to the automatic stay otherwise imposed on all actions against the debtor, 11 U.S.C. § 362(a), for "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power." *Id.* § 362(b)(4). The exception applies "where a governmental unit is suing a debtor to prevent or stop violation of . . . environmental protection . . . laws, or attempting to fix damages for violation of such a law." S. Rep. No. 989, 95th Cong., 2d Sess. 52, reprinted in 1978 U.S. Code Cong. & Ad. News 5838. *See Penn Terra, supra*, slip op. at 15-25 (injunction to enforce compliance with state environmental protection laws is not money judgment, is not subject to § 362 stay); *Commonwealth v. Peggs Run Coal Co.*, 55 Pa. Cmwlth. 312, 923 A. 2d 765 (1980) (same); *cf. In re Canarico Quarries, Inc.*, 466 F. Supp. 1333, 1339-40 (D.P.R. 1979) (case under old law using new § 362(b)(4) as persuasive authority to hold not stayed a proceeding to enforce compliance with Federal Clean Air Act, 42 U.S.C. § 7401-7642 (1976)). *See also In re Kovacs*, 681 F.2d 454, 456 (6th Cir. 1982) (discussed in *Penn Terra, supra*, slip op. at 22 n.11), *vacated and remanded on other grounds*, 103 S. Ct. 810 (1983), *on remand sub nom. Ohio v. Kovacs*, 717 F.2d 985 (6th

Cir. 1983), *cert. granted*, No. 83-1020, 52 U.S.L.W. 3650 (U.S. March 5, 1984).

A second indication that the bankruptcy scheme is not intended to abrogate relevant state laws is found in 28 U.S.C. § 959(b) (1982):

> (b) Except as provided in section 1166, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

The trustee in this case argues that Section 959(b) is inapplicable outside a chapter 11 proceeding (Br. at 12), where the trustee is managing the debtor's business, *see* 11 U.S.C. § 1108 (1982). Even in a chapter 7 proceeding, however, the trustee may be authorized to operate a business. *Id.* § 721. Thus there is no reason to suppose Section 959(b) inapplicable in chapter 7.

Implicit in Section 959(b) is the notion that the goals of the federal bankruptcy laws, including rehabilitation of the debtor, do not authorize transgression of state laws setting requirements for the operation of the business even if the continued operation of the business would be thwarted by applying state laws. *See Gillis v. California*, 293 U.S. 62 (1934); *In re Dolly Madison Indus.*, 504 F.2d 499 (3d Cir. 1974); *In re Canarico Quarries, Inc.*, 466 F. Supp. 1333 (D.P.R. 1979). New York argues that this principle extends to the liquidation process, contending that the goal of the federal bankruptcy law here -- distribution of the assets to creditors -- does not

authorize transgression of state laws setting requirements for disposal of assets.

Our examination of Section 959(b) leads us to conclude that although it is not itself an independent prohibition of the trustee's abandoning property in contravention of state law, it is a clear indication that in general the congressional scheme was not intended to subjugate state and local regulatory laws. As a matter of simple statutory construction, the applicability of Section 959(b) would seem open to question. The provision speaks in terms of "manage[ment]" and operat[ion] of the "property." It would not strain the language to construe "management of the property" to include abandonment of a facility. Nor would it be a gross misreading to construe "manage and operate" narrowly, to mean only the administration of the business as a going concern. Again, we have found no legislative history.

Section 959(b) refers to the railroad reorganization provisions of the Bankruptcy Act; these permit the court to authorize abandonment of a line if it is consistent with the public interest. 11 U.S.C. § 1170(a). But since railroad reorganization is treated as *sui generis* within the Act, *see* 11 U.S.C. § 1161, this reference is of little relevance to the inquiry except as it indicates that state laws are not applicable to abandonment of a railroad line (although the extent of their applicability in determining the public interest is not indicated).

The trustee cites two authorities for support of a narrow construction of the provision. One is a footnote in *Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 778 n. 18 (8th Cir. 1981), in which the court stated, in dictum and without analysis, its "doubt" that a Chapter XI trustee for a grain elevator would be prohibited from selling grain in the exercise of his

power to liquidate assets even though state law required a license to sell grain. By contrast the trustee would, by Section 959(b), be required to obtain a state license to operate the grain warehouses. *Id.* at 778. This case would seem to be authority for a distinction between operation of a business and liquidation of its assets. There was, however, no showing that failure to comply with the state law in question would in any way affect the public health, safety, or welfare, in contrast to the case here. Would the 8th Circuit have so readily dismissed the issue if the trustee had been selling spoiled grain, in contravention of state law? Its terse statement is devoid of analysis and is therefore of little help to the trustee's cause here.

The trustee also relies, as did the court below, on a statement in a treatise:

> But § 959(b) applies only to the receiver in his operation of the property in his possession. It does not require the federal receivership court to comply with state laws regulating the distribution of funds in receivership, although *Erie R. Co. v. Tompkins* should now require it to do so in cases involving only non-federal matters.

7-pt 2 Moore's Federal Practice, ¶ 66.04[4] at 1913 (J. Moore & J. Lucas 2d ed. 1982) (footnotes omitted). This paragraph is authority for a basic distinction between distribution of funds in liquidation and operation of a business. Again, though, its reach is limited. Clearly state law regulating the distribution of assets among creditors must give way to the all-encompassing federal law of creditors' rights. *American Surety Co. v. Sampsell*, 327 U.S. 269, 272 (1946). It does not follow that state police power regulations must also give way.

Chicago Transit, supra, 129 F.2d at 6, noted that prohibiting abandonment in that case while

permitting the trustee to cancel the lease would not violate the predecessor to Section 959(b), 28 U.S.C. § 124 (1940), which required that federal receivers operate trust property in accordance with the laws of the state as the owner would be bound to do. There would be no violation because the trustee was ordered to comply with state law to the extent it required service to be continued; but the state's authority could not be extended to the protection of existing contracts, rather these could be abrogated by the court in its exercise of equitable powers.

Chicago Transit, however, is not precisely on point here: the state law required operation of the business, whereas New York law here only limits abandonment (disposal) of the facilities and does not speak to operation of the business. Thus the *Chicago Transit* case does not answer the inquiry whether Section 959(b) applies outside of the operation of a business (or maintenance of its assets in anticipation of such). But it would be an overly literal reading that would dismiss wholly the import of the provision on the ground that "abandonment" of property is distinguishable from "management" of property. The interests at stake are not so different; in each case the creditors have an interest in preserving the debtor's estate so as to maximize their proportionate recovery; indeed, when the debtor's business is managed on a chapter 11 proceeding, there is another interest to be considered, the debtor's interest in rehabilitating the business as a going concern. Thus, since courts have been willing to find Section 959(b) applicable even if these two interests are thwarted, *a fortiori* it is not inapplicable just because one interest is adversely affected.

Thus, at the very least, the existence of Section 959(b) indicates that Congress has not "unmistakably ordained" that state law is superseded by the trustee's powers to administer the property of the estate.

The third, and final, consideration that informs our decision is the provision in the bankruptcy act for the application of equitable principles to determine the efficacy of requested relief. In addition to the powers given to the court in 11 U.S.C. § 105 to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions" of the Act, 28 U.S.C. § 1481 establishes the jurisdiction of the court to include all the powers of a court of equity.[8] Under the old bankruptcy statute, under which bankruptcy courts had been given "such jurisdiction at law and equity as will enable them to exercise original jurisdiction," 11 U.S.C. § 2 (1976) (repealed) it was held that bankruptcy courts are courts of equity and may apply equitable doctrines and principles insofar as they are consistent with the statute. *SEC v. United States Realty Co., supra*, 310 U.S. at 455; *Pepper v. Litton*, 308 U.S. 295, 304-05 (1939).

This same proposition has been held applicable to the 1978 Act: "[B]ankruptcy courts are courts of equity, but at the same time, authorized to prevent courses of conduct otherwise fraudulent, abusive or unfair." *In re Multiponics, Inc.*, 622 F.2d 709, 721 (5th Cir. 1980) (citations omitted, but citing *Pepper v. Litton, supra*).

Thus, since there is no unmistakable evidence of congressional intent to abrogate the enforcement of state environmental protection laws -- rather, there is evidence of an intent to accommodate such laws -- and since equitable principles must be applied, federal law is supreme only if those principles demand that state

8. Section 1481 did not technically become effective until April 1, 1984, but transition provisions of the Bankruptcy Reform Act vest courts with the same authority they would have as of that date. *See* Pub. L. No. 598, 95th Cong., 2d sess. § 405(b) (1978); *Universal Minerals, Inc. v. C. A. Hughes & Co.*, 669 F.2d 98, 100 n.2 (3d Cir. 1981).

police powers be suspended to the extent they interfere with the liquidation of the estate.

C.

The cases discussed *supra* that stand for the proposition that equitable principles are applicable in determining whether a trustee may abandon property in contravention of state law require that a court balance the relative weight of the state and federal policies. In this case, the state and local regulations advance a very important policy: to protect the public health by regulating disposal of toxic wastes. Abandonment by the trustee clearly contravened applicable law, and did so not merely technically, but with severely deleterious implications for the public safety. The great weight thus attaching to the state's interest makes this case more akin to those of *Ottenheimer v. Whitaker, supra*, and *In re Lewis Jones, supra*, than it is to *In re Adelphi Hospital*. The weight of state law is reflected also in the fact that (as in *Ottenheimer*) violation of the disposal regulations may constitute a felony. *See* N.Y. Envtl. Conserv. Law § 71.2721 (McKinney Supp. 1982).

To be weighed against this manifestly important public policy is the policy advanced by abandonment, to preserve as much of the estate as possible for distribution to creditors. This policy must be viewed in light of the indications of a concurrent federal legislative policy to limit intrusion into state police power regulations, including environmental protection laws, delineated *supra*. Here, it is undisputed that compliance with hazardous waste disposal laws required substantial expenditures, thus depleting the assets of the estate available for distribution to creditors.

But the extent (unproven in these proceedings)[9] of the expenditures necessary to dispose of the waste properly is not in itself sufficient to outweigh the public interest at stake here. It is only recently that the public has learned of the magnitude of the dangers associated with toxic waste disposal; at the same time, the last few years have witnessed a rising tide of bankruptcies. Lurking in the shadows of these phenomena is the spectre of the changing fortunes of the nuclear power industry, with the concomitant potentiality for unusable facilities. If trustees in bankruptcy are to be permitted to dispose of hazardous wastes under the cloak of the abandonment power, compliance with environmental protection laws will be transformed into governmental cleanup by default. It cannot be said that the bankruptcy laws were intended to work such a radical change in the nature of local public health and safety regulation -- the substitution of governmental action for citizen compliance -- without an indication that Congress so intended.[10] The

9. The issue of the exact amount of the depletion was never brought before the bankruptcy court, or the district court. The Trustee alleged that the property itself had a fair market value of $535,000, and a forced sale value of $428,000, both at the time subject to mortgages in excess of $450,000. Tr. of June 8, 1982 Bankruptcy Hearing at 2. But this does not relate the expense to the size of the debtor's estate. The Trustee did note that at the time he was unable to liquidate some major assets (such as oil). *Id.* at 11-12.

10. Indeed, Congress has elsewhere indicated an intent that governmental units be reimbursed, by those responsible for storage, transport, and disposal of hazardous wastes, for government's costs of emergency cleanup of inactive hazardous waste sites by creating a federal cause of action for reimbursement. Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. § 9607 (Supp. V 1981) ("superfund"

supremacy clause does not require the suspension of the operation of New York's hazardous waste disposal laws.[11]

III.

New York requests that it be reimbursed, out of the assets of the estate, for its cleanup costs as an

legislation); one objective of imposing liability was "to induce such [liable] persons *voluntarily to pursue appropriate environmental response actions* with respect to inactive hazardous waste sites." H. Rep. No. 1016, Pt. I, 96th Cong. 2d Sess. 17 (1980), reprinted in 1980 U.S. Code Cong. & Ad. News 6120 (emphasis added).

11. As support for its basic position that the abandonment power is not limited by state law, and not as a separate or discrete issue or independent bar to the enforcement of state law, the Trustee contends that prohibiting abandonment may effect an unconstitutional taking under the Fifth Amendment. The Trustee argues that use of the estate's assets to comply with state law may deplete the estate to such an extent that the secured creditors will receive less in satisfaction of their claims than they otherwise would have.

The rights of a secured creditor in the debtor's assets are "property" subject to a "taking." *See United States v. Security Indus. Bank*, 103 S. Ct. 407, 411 (1982). But we are not persuaded by the Trustee's argument that an unconstitutional taking could result from forbidding abandonment here. First, the state's enforcement of its environmental protection laws cannot be characterized as a taking; rather it is a permissible exercise of the state's regulatory power to promote the public good, under a long line of cases dealing with just that distinction. *E.g., Agins v. City of Tiburon*, 447 U.S. 255 (1980) (municipal zoning ordinances restricting type and density of buildings held not a taking); *Penn Central Transp. Co. v. City of New York*, 438 U.S. 104 (1978) (landmark preservation ordinance); *Goldblatt v. Hempstead*, 369 U.S. 590 (1962) (town ordinance prohibiting use of land for mining); *Miller v. Schoene*, 275 U.S. 272 (1928) (statute requiring landowner to destroy diseased cedar trees); *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365 (industrial zoning regulation); *Hadecheck v. Sebastian*, 239 U.S. 394 (1915) (municipal ordinance prohibiting brickmaking); *Mugler v. Kansas*, 123 U.S. 623 (1887) (state statute declaring places of manufacture of liquor

"administration expense," *see* 11 U.S.C. §§ 503(b) & 507(a).

Section 503(b) lists several categories of allowable administrative expenses. The categories are not exclusive: administrative expenses "including" those listed are allowed, and "including" is not exclusive, 11 U.S.C. § 102(3). The only relevant category of those listed would seem to be Section 503(b)(1)(A), "actual, necessary costs of preserving the estate." Preservation

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to be nuisances); *Troy v. Renna*, 727 F.2d 287 (3d Cir. 1984) (state statute creating statutory tenancies for senior citizens and disabled persons). *See generally* Michelman, Property, Utility, and Fairness: Comments on the Ethical Foundations of "Just Compensation" Law, 80 Harv. L. Rev. 1165, 1183-84 (1967) (factors relevant to classifying an action as regulation or taking).

Second, the Trustee contends that this case presents the possibility of an "erosion taking," citing to the *Regional Reorganization Act Cases*, 419 U.S. 102 (1974), and *In re New York, N.H. & H .R.R.*, 330 F. Supp. 131, 147 (D. Conn. 1971), *rev'd on other grounds*, 457 F.2d 683 (2d Cir. 1972) (lack of subject matter jurisdiction); *see also New Haven Inclusion Cases*, 399 U.S. 392 (1970). The doctrine in those cases, even if deemed to be applicable here (and we have serious doubts that it would be applicable, because of the sui generis nature of the subject matter, railroad reorganization) would require a balancing of the losses to the estate against the public interest. Whether an erosion taking will result would depend under this theory on whether forcing expenditure of assets by preventing abandonment will cause "losses unreasonable even in light of the public interest." *Regional Railroad Reorganization Act Cases, supra*, 419 U.S. at 124 (taking by accrual of post-bankruptcy claims with priority over those of claimants). We cannot say that the public interest would be outweighed by losses here. Our prior analysis applies with equal force here in determining whether it is constitutionally "unreasonable" to require that the estate's assets be expended to comply with toxic waste disposal law as a condition of abandonment. *Cf. City of Paterson v. Fargo Realty, Inc.*, 174 N.J. Super. 178, 415 A.2d 1210 (1980) (not unconstitutional to require owner to reimburse city for expenses incurred in razing structure that was public nuisance).

includes the costs of custodial care or insurance, *see* 3 Collier on Bankruptcy (L. King 15th ed. 1983), *supra*, ¶ 503.04 at 503-16, and necessary repairs, *id.* We need not, however, reach the issue of the priority, if any, of New York's claim. That is an issue that can properly be resolved only by the bankruptcy court, since the issue was not treated in the proceedings below and so the record on appeal does not include findings of relevant fact.

IV.

The order of the district court dated January 25, 1983, which affirmed the order of abandonment will be reversed, and the case remanded for proceedings consistent with this opinion.

Each party will bear its own costs.

GIBBONS, *Circuit Judge*, dissenting:

The majority opinion poses as the issue in this case whether 11 U.S.C. § 554 (1982) "permit[s] the abandonment of property of the bankrupt estate in contravention of state and local environmental protection laws?" Maj. op., typescript at 3. In focusing on this single issue, however, the majority fails to consider additional points of extreme relevance to this case.

State and local environmental protection laws simply do not address federal bankruptcy law interests, including whether and under what circumstances the trustee of a debtor's estate must take possession of all property in the estate. After all, trustees are creatures of federal law. They are appointed not for the benefit of the world at large, but solely for the purpose of liquidating property for the benefit of creditors, a federal interest. *See* 11 U.S.C. § 704 (1982). Some state environmental protection laws, like those of New York, attempt to impose expenses on the debtor's estate that

would leave no equity to be liquidated. In this case, for example, it is undisputed that New York law would leave the debtor's estate with no actual or potential equity in the Long Island City property. By forcing the trustee to take possession of property in which there is no equity, the court serves no interest that the bankruptcy laws address. By not confronting that reality, the majority opinion fails to resolve critical issues in this case: how can the trustee reach into the creditors' pockets for the cost of the cleanup, and if he can, which creditor's pocket?

The proper analysis must begin with the relevant statute and the question of the trustee's right to abandon the property. Section 554 of title 11 states clearly:

> (a) After notice and a hearing, the trustee may abandon any property of the estate that is burden some to the estate or that is of inconsequential value to the estate.

11 U.S.C. § 554(a) (1982). There is no legislative history suggesting that we may alter or amend that language. The intent is clear. The record here establishes that the property is burdensome and of inconsequential value to the estate. A finding by the bankruptcy court to that effect has not been challenged on appeal. Thus, under federal law, the trustee may abandon the property.

This point is challenged, however, by the State and City of New York, who argue that such abandonment cannot be permitted when it would violate the public interest and federal, state and local environmental laws. Appellants cite for support a Fourth Circuit and a bankruptcy court case for the proposition that abandonment may be denied when such abandonment would threaten public health and safety and/or violate federal law. The cases presented by appellants are *Ottenheimer v. Whitaker*, 198 F.2d 289 (4th Cir.), *aff'g*

102 F. Supp. 913 (D. Md. 1952), and *In re Lewis Jones*, 1 B.C.D. 277 (Bk. Ct. E.D. Pa. 1974).

Neither of these opinions, however, is persuasive under the 1978 Bankruptcy Reform Act. Both substitute slogans about equity for an analysis of the purpose of bankruptcy proceedings. Both, moreover, were decided prior to the enactment of the Bankruptcy Reform Act of 1978, and its codification in 11 U.S.C. § 554 (1982) of the express authority for trustees to decline to undertake responsibility for property which cannot benefit the estate. Thus there was no statutory provision permitting trustees to abandon burdensome property at the time of those decisions. Such an express statutory provision now exists. Moreover, Congress did *not* see fit to provide an exception to this statutory power, whether for the public interest or any other purpose, as it has in other areas. *Compare* 11 U.S.C. § 362(a) (1982) (exception to automatic stay); *Penn Terra Ltd. v. Department of Environmental Resources*, 733 F.2d 267, 274-79 (3d Cir. 1984) (injunction to enforce compliance with state laws is not a money judgment, and is therefore not subject to § 362 stay) *with* 11 U.S.C. § 554 (1982). Thus *Ottenheimer* and *Lewis Jones* are not helpful.[1]

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1. Both cases acknowledge that the rules regarding abandonment in their case were judge-made:

> It seems obvious to us that a rule which is not provided by statute but built up by the courts to facilitate the administration and distribution of the assets of a bankrupt estate should not be extended so as to reach such an unreasonable and unjust result. The judge-made must give way when it comes into conflict with a statute enacted to ensure the safety of navigation
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> . . .

Ottenheimer, 198 F.2d at 290; *see Lewis* 1 B.C.D. at 279; *see also* Missouri v. United States Bankruptcy Court, 647 F.2d 768, 778 n.18 (8th Cir. 1981) (doubtful tht trustee could be prevented from

The majority opinion is also inconsistent with the Supreme Court's recent decision in *United States v. Security Industrial Bank*, 103 S. Ct. 407 (1982). There the Supreme Court held that the Bankruptcy Act should not be construed to destroy the interests of creditors when a substantial question arises as to whether the Act constitutes a taking of property without just compensation. The holding in *Security Industrial Bank* is simply a corollary of the longstanding doctrine that we are obliged "first [to] ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided." *United States v. Security Industrial Bank*, 103 S. Ct. at 412 (*quoting Lorillard v. Pons*, 434 U.S. 575, 577 (1978) and *Crowell v. Benson*, 285 U.S. 22, 62 (1932)). Similarly, "in the absence of a clear expression of Congress' intent . . . [a court should] decline to construe the Act in a manner that could in turn call upon the Court to resolve difficult and sensitive questions arising out of the guarantees of the takings clause." *Security Industrial Bank*, 103 S.Ct. at 414 (*quoting NLRB v. Catholic Bishop of Chicago*, 440 U.S. 490, 507 (1979)).

The Supreme Court has indicated that creditors cannot be forced to operate a business, no matter how vital to the public interest, at a loss. *See Railroad Commission of Texas v. Eastern Texas Railroad Company*, 264 U.S. 79, 85-86 (1924); *Brooks-Scanlon Co. v. Railroad Commission of Louisiana*, 251 U.S. 396, 399 (1920); *see also Regional Railroad*

selling grain to liquidate assets even though state law requires license to do so); In re Adelphi Hospital Corp., Bank. L. Rep. (CCH) ¶ 66,882, at 76,856 (2d Cir. 1978) (bankrupt hospital's trustee can abandon medical records even though state law requires their maintenance); *see generally* In re Chicago Rapid Transit Co., 129 F.2d 1, 5 (7th Cir.), *cert. denied*, 317 U.S. 683 (1942) (pre-statute case stating withdrawal of state power should be stated in Act).

Reorganization Act Cases, 419 U.S. 102, 122 (1974); *Bullock v. Railroad Commission of Florida*, 254 U.S. 505, 520-21 (1921). In the *Regional Railroad Reorganization Act Cases*, the Supreme Court did not "balance" the interest of creditors against that of the public. *See* 419 U.S. at 122-36. The Court upheld the Regional Railroad Reorganization Act only because there was an available remedy in the Tucker Act, 28 U.S.C. § 1491 (1982), for the operational losses which that Act imposed. 419 U.S. at 136. New York does not suggest that its law provides an equivalent remedy. The name of its game is transferring the cost of cleanup to secured and unsecured creditors of the debtor, in this instance outside New York, who have no interest whatever in the Long Island City property, and who, on the record before us, were in no way responsible for placing the contaminated oil on that site.

Thus, the majority's construction of the Act raises a substantial question under the taking clause of the fifth amendment.[2] The holding of *Security Industrial*

2. The "taking" concern has been raised previously:

> [T]he public interest cannot demand the erosion of the bankrupt's assets to the point of confiscating practically the entire estate. At some point the extent and degree of taking runs into the constitutional prohibition in the Fifth Amendment [on] the taking of private property for public use without just compensation.

In re New York, New Haven and Hartford Railroad Co., 330 F. Supp. 131, 147 (D. Conn. 1971); *see also* H.R. Rep. No. 595, 95th Cong., 1st Sess. 423 (1977), *reprinted in* 1978 U.S. Code Cong. & Ad. News, 5963, 6379:

> Subsection (a) [11 U.S.C. § 1170(a)] permits the court to authorize the abandonment of a railroad line if the abandonment is consistent with the public interest and either in the best interest of the estate or essential to the formulation of a plan . . . The authority to abandon or

Bank compels a construction of section 554 that avoids this difficult constitutional issue. Such a construction is available, for the plain language of that section permits abandonment in this case; moveover, there is no legislative history to that section providing any exceptions to the statute or expressing any intent contrary to abandonment by a trustee of property found to be burdensome or of inconsequential value. A fair reading of section 554 permits abandonment in this case and thus avoids the constitutional question presented by the taking clause.

The majority opinion deals with the taking problem in a footnote. Maj. op., typescript at 26 n.ll. That footnote, however, puts the rabbit in the hat by concluding perfunctorily that the New York statutes at issue constitute a "regulation" rather than a "taking" of property.[3] That is not the analysis of *Security Industrial Bank.* The Supreme Court requires that we address whether a substantial question under the taking clause arises; the *Regional Railroad Reorganization Act Cases* raise such a question. We are therefore required to construe the Bankruptcy Act accordingly.

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not to abandon lines of railroad is, of course, subject to the fifth amendment of the Constitution, which may in particular cases require abandonment in order not to erode a secured creditor's interest in the debtor's property even though the public interest dictates otherwise.

3. In its taking analysis, the majority opinion characterizes the environmental protection laws as an example of "the state's regulatory power to promote the public good" (citing cases). Maj. op., typescript at n. ll. The cases cited, however, do not address the question of imposing an obligation on third parties. Thus the police power cases are irrelevant to the issue of an obligation on the part of innocent creditors to undertake compliance with the police power statutes.

The majority opinion sidesteps a key issue by stating that "we need not . . . reach the issue of the priority, if any, of New York's claims." Maj. op., typescript at 28.[4] Yet, the record is unequivocal. The debtor's estate has no equity whatever in the Long Island waste oil storage facility. Thus the necessary implication of the majority's holding is that property situated elsewhere must be expended for the purpose of complying with the New York toxic waste laws. Whether that expenditure is justified because New York law imposes a lien or charge on property situated elsewhere or because New York law requires that the expenditures be treated as costs of administration under ll U.S.C. §§ 503(b), 507(a) (1982), the outcome is the same, for the majority's opinion cannot conceal the patent reality that the cost of cleaning the Long Island City site must come from someone's pocket. Remanding without addressing the question of whose pocket is irresponsible.

The majority's reliance on 28 U.S.C. § 959(b) (1982) is off the mark. If the trustee, or any other court officer, undertook to *operate* the Long Island facility, that officer would be required to operate it in compliance with local police power regulations by virtue of section 959(b). But section 959(b) cannot be construed as imposing an obligation to operate *any* business or property. In proceedings for reorganization or liquidation a trustee will undertake to operate a business or property only when such operation can inure to the benefit of some party having an interest in the estate. Were section 959(b) to be construed otherwise it would violate the fifth amendment

---

4. The majority opinion appears to refer to an affidavit stating that some parties with priority liens relinquished them in favor of a first lien sought by the State and City. *See* Affidavit of Nancy Stearns, December 22, 1982.

prohibition against taking without just compensation. *Regional Railroad Reorganization Act Cases*, 419 U.S. 102, 118, 125 (1974); *see United States v. Security Industrial Bank*, 103 S.Ct. 407, 411 (1982) (secured creditor's rights in debtor's assets are "property" subject to "taking").[5]

The majority's argument is not advanced by its observation that "[t]he supremacy clause does not require the suspension of New York's hazardous waste disposal laws." Maj. op., typescript at 26. Those laws are not suspended by the district court's disposition. They have operated so as to eliminate any interest that the debtor's estate might have had in the Long Island City plant. They may result in criminal prosecution of the persons actually responsibile for placing the toxic substances on the site. *See, e.g.*, N.Y. Envtl. Conserv. Law § 71.2721 (McKinney Supp. 1982). Moreover, those laws do not by their terms give fair notice to secured and unsecured creditors of the debtor that *they* would become liable for the cost of cleanup merely by extending credit to a corporation which unknown to

5. There is further evidence of doubt as to whether section 959(b) applies to Chapter VII proceedings. Professor Moore stated:

> [Section] 959(b) applies only to the Receiver in his operation of property in his possession. It does not apply to the distribution of the estate, and does not require the federal receivership court to comply with state laws regulating the distribution of funds in the receivership . . .

7 J. Moore & J. Lucas, Moore's Federal Practice § 66.04(4), at 1913 (2d ed. 1982). Moreover, although a trustee may be authorized to operate a business under section 721, such operation may occur only "for a limited period" and only "if such operation is *in the best interest of the estate* and consistent with the orderly liquidation of the estate." 11 U.S.C. § 721 (1982) (emphasis suplied). Such authorization here clearly would not be in the best interests of the estate.

them should in the future violate the law. Nor do they give notice to a trustee in bankruptcy that he would, merely by virtue of his appointment, become responsibile for undoing the effects of a debtor's prior unlawful activities.

Without definitely resolving the question, the majority suggests that 11 U.S.C. § 503(b)(1)(A) (1982), dealing with allowable costs of administration, and 11 U.S.C. § 102(3) (1982), dealing with an expansive rule of construction, may authorize the imposition of cleanup costs on other creditors. Maj. op., typescript at 27-28. The suggestion that the cleanup cost might be classified as a "preservation expense" of a property is preposterous. Upon abandonment, title to the property revests in the bankrupt. Fiduciaries are not at liberty to "preserve" the property in which their cestui have no interest. The reference to the court's "equitable" powers, Maj. op., typescript at 22-24, assumes that the court has "equitable" power to compel the operation of a business at a loss in the public interest. As discussed earlier, the taking clause of the fifth amendment, applicable to the states by virtue of the fourteenth, prevents the exercise of any such "equitable" power. Before the trustee may incur expenses of administration to which section 102(b) may apply, there must be an identifiable source of authority for making such expenditures. None exists.

Finally, the majority remands to the district court with no guidance about the critical issues in this case. That court has already determined that New York law does not and, in light of the supremacy clause, cannot compel a trustee in bankruptcy to undertake possession or operation of a business from which the estate can derive no benefit. On remand the court will still be at a loss to determine how, consistent with the taking clause, the trustee can reach into the creditors' pockets for the cost of cleanup, and if he can, which

creditors' pockets. The majority remands with no more than a hope that the court can get money somewhere.

Since the record is clear that the debtor's estate does not have any actual or potential equity in the Long Island City property, and New York has not pointed to any other specific property on which it has a valid lien for the cost of cleanup of that site, the district court did not err in authorizing abandonment. Certainly that order was not an abuse of discretion. Nowhere does the majority disclose what alternative course might have been pursued. I would affirm now, as we surely will have to affirm later, when the district court points to the obvious fact that there must be a source of funds before expenditures can be made.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit

APPENDIX B

Opinion of the United States Court of Appeals for the Third Circuit (No. 83-5730)

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 83-5730

IN RE: QUANTA
RESOURCES CORPORATION

Debtor

THE NEW JERSEY DEPARTMENT OF
ENVIRONMENTAL PROTECTION

Appellant

On Appeal from the United States
Bankruptcy Court for the
District of New Jersey

(Bankruptcy No. 81-05967)

Submitted Under Third Circuit Rule 12(6)
June 19, 1984

Before: GIBBONS, GARTH and
HIGGINBOTHAM, *Circuit Judges*

(Opinion Filed July 20, 1984)

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OPINION OF THE COURT

GARTH, *Circuit Judge.*

This appeal presents us with the identical issue presented by the companion case of *In re Quanta*

Resources Corp. (City of New York and State of New York v. Quanta Resources Corp.), No. 83-5142. Because we have decided to reverse the district court's order in the companion case, in which New York was the appellant, we will also reverse the bankruptcy court's order in this case.

I.

Quanta Resources Corp. (Quanta) leased and operated a facility on a site in Edgewater, New Jersey, at which Quanta processed and resold waste oil and oil sludge. Quanta operated the site under "temporary operating authorities" (TOA's) issued by the New Jersey Department of Environmental Protection (NJDEP). These TOA's prohibited Quanta from accepting PCB-contaminated oil.

On June 23, 1981, NJDEP found PCB-contaminated oil at the site. On July 2, 1981, Quanta agreed to cease operating at the Edgewater location. On October 6, 1981, while NJDEP and Quanta were negotiating as to Quanta's obligation to clean up the contaminated oil, Quanta filed a petition in bankruptcy under chapter 11 of the Bankruptcy Code, an action which was later (on November 12, 1981) converted to a chapter 7 liquidation. On October 7, 1981, NJDEP issued an administrative order requiring Quanta to cease operations, close the facility within one year, and clean up all hazardous materials.

On April 23, 1983, the Trustee for Quanta gave notice of proposed abandonment of the facility under 11 U.S.C. § 554 of the Bankruptcy Code, including the waste oil contained in tanks. The Trustee excepted from this notice that part of the oil which was free of significant contamination from PCB's and was the subject of a pending sale agreement.

NJDEP opposed the abandonment, arguing that the abandonment would violate New Jersey law

because oil contaminated with PCB's must be stored and disposed of in compliance with state regulations. According to the state, abandonment would contravene these requirements and pose a threat to public health and safety because the oil was stored in leaking and insecure tanks, creating a danger of spillage into the Hudson River. NJDEP argued that the estate had sufficient funds to protect the public from the hazards.

After a hearing, by order dated May 20, 1983, the Bankruptcy Court authorized the requested abandonment of the oil, the order stating that its entry was to "be deemed to constitute the abandonment of the . . . property by the Trustee effective May 17, 1983, *nunc pro tunc.*" *In re Quanta Resources Corp.*, No. 81-05967 (Bankr. D.N.J. May 20, 1983). The sale of the remaining oil was completed in June 1983, and the Trustee vacated the premises on July 1, 1983.

The parties consented to NJDEP's taking a direct appeal to this court under 11 U.S.C. § 405(c)(1)(B). We therefore have appellate jurisdiction. *See* 28 U.S.C. § 1293(b) & note preceding *id.* § 1471 (appellate jurisdiction to consider such appeals).

II.

The instant case does not present us with a significantly different factual situation from that presented to us in *In re Quanta Resources Corp.*, No. 83-5142. In this case, abandonment of the property and the toxic oils will effect a disposal of toxic waste in a manner that contravenes New Jersey environmental protection law.[1] There is no principled distinction

1. NJDEP argues that federal environmental law is also violated by the abandonment. Since NJDEP has not persuaded us that it has the power to enforce federal law in this situation, there is no issue before us as to a conflict between the abandonment power under § 554 of the Bankruptcy Code and federal environmental protection law.

between the issues presented in this case and those presented in the companion *Quanta* case in which New York is the appellant. Thus the analysis and reasoning of No. 83-5142 apply equally to the case at bar. We hold that the Trustee does not have the right to abandon property of the estate where abandonment contravenes state public health and safety laws, as it does here.

Because NJDEP -- unlike the City and State of New York in the companion case at 83-5142 -- has not argued that it should be reimbursed for any expenses incurred in cleaning up or restoring the property (indeed NJDEP has not asserted that it incurred any such expenses),[2] we have no cause to address that issue. This point serves to emphasize the scope of our central holding in these two cases -- that enforcement of state public health and safety laws is not superseded by the power of abandonment contained in section 554 of the Bankruptcy Code. The issue is not who should pay to clean up the estate's property; it is whether the Trustee's interest in preserving the estate should prevail over the public's interest in containing the hazards produced by toxic wastes in the possession of the estate. As in the companion case where the State and City of New York are appealing, we are convinced that the equities must be balanced in favor of the public interest.

III.

The bankruptcy court's order authorizing abandonment of the estate's property at the Edgewater site will be reversed and the case remanded to the

2. NJDEP did claim an interest in the property prior to abandonment, as did Midlantic National Bank, an appellee here. However, the nature of that interest has not been disclosed to us and it is not a factor for consideration on this appeal.

bankruptcy court for further appropriate proceedings in light of both *Quanta* opinions.

GIBBONS, *Circuit Judge*, dissenting:

The same issue is before us as was presented in the companion case *In re Quanta Resources Corp. (City of New York and State of New York v. Quanta Resources Corp.)*, No. 83-5142. I would affirm the bankruptcy court's order in this case for the same reasons stated in my dissent in the companion case.

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit

APPENDIX C

Orders Amending Opinion (No. 83-5730)

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 83-5730

IN RE: QUANTA RESOURCES CORPORATION

Debtor

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION

Appellant

Before: GIBBONS, GARTH and HIGGINBOTHAM, *Circuit Judges*

ORDER AMENDING OPINION

IT IS ORDERED that the opinion in the above-captioned matter, filed July 19, 1983, is hereby amended as follows:

Add, immediately after the last sentence of the opinion, the following new paragraph:

Each party will bear its own costs.

BY THE COURT,

Leonard I. Garth

Circuit Judge

DATED: July 25, 1984

Appendix C

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit

(A.O. U.S. Courts. G.M.C. Printing, Phila., Pa. 215-568-4264)

Appendix C

UNITED STATES COURT OF APPEALS
FOR THE THIRD CIRCUIT

NO. 83-5730

IN RE: QUANTA
RESOURCES CORPORATION

Debtor

THE NEW JERSEY DEPARTMENT OF
ENVIRONMENTAL PROTECTION

Appellant

On Appeal from the United States
Bankruptcy Court for the
District of New Jersey

(Bankruptcy No. 81-05967)

Submitted Under Third Circuit Rule 12(6)
June 19, 1984

Before: GIBBONS, GARTH and
HIGGINBOTHAM, *Circuit Judges*

(Opinion Filed July 20, 1984)

ORDER

It is ORDERED

That so much of the designation of attorneys for the appellant that appears on the cover of the above entitled opinion be amended to read as follows:

Appendix C

Irwin I. Kimmelman
Attorney General of New Jersey
James J. Ciancia
Assistant Attorney General
Richard F. Engel
Deputy Attorney General
Ross A. Lewin, Esq.
Deputy Attorney General

By the Court

/s/ Leonard I. Garth
United States Circuit Judge

Dated: August 17, 1984

A True Copy:

Teste:

Clerk of the United States Court of Appeals for the Third Circuit

(A.O. U.S. Courts. G.M.C. Printing, Phila., Pa. 215-568-4264)

APPENDIX D

Judgment of the United States Court of Appeals for the Third Circuit (No. 83-5142)

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 83-5142

IN THE MATTER OF

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

Debtor

CITY OF NEW YORK and
THE STATE OF NEW YORK

vs.

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

State of New York and City of New York,

Appellants

(D. C. Civil No. 82-3524)

Appendix D

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF NEW JERSEY, Newark

Present: GIBBONS, GARTH and HIGGINBOTHAM, *Circuit Judges.*

JUDGMENT

This cause came on to be heard on the record from the United States Bankruptcy Court for the District of New Jersey, Newark and was argued by counsel October 24, 1983.

On consideration whereof, it is now here ordered and adjudged by this Court that the judgment of the said District Court, entered January 25, 1983, be, and the same is hereby reversed and the cause remanded for further proceedings consistent with the opinion of this Court. Each party to bear its own costs.

ATTEST:

SALLY MRVOS
Clerk

July 20, 1984

Certified as a true copy and issued in lieu of a formal mandate on August 28, 1984.

Test:

M. ELIZABETH FERGUSON
Chief Deputy Clerk, United States Court of Appeals for the Third Circuit.

APPENDIX E

Judgment of the United States Court of Appeals for the Third Circuit (No. 83-5730)

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 83-5730

IN RE:

Quanta Resources Corporation,
Debtor

The New Jersey Department of Environmental Proection,
Appellant

(Bankruptcy No. 81-05967)

ON APPEAL FROM THE UNITED STATES BANKRUPTCY COURT FOR THE DISTRICT OF NEW JERSEY, Newark

Present: GIBBONS, GARTH and HIGGINBOTHAM, *Circuit Judges.*

Appendix E

AMENDED JUDGMENT

This cause came on to be heard on the record from the United States Bankruptcy Court for the District of New Jersey and was submitted under Third Circuit Rule 12(6) on June 19, 1984.

On consideration whereof, it is now here ordered and adjudged by this Court that the order of the said District Court filed May 20, 1983 be, and the same is hereby reversed and the cause remanded to the said Bankruptcy Court for further appropriate proceedings in light of this Court's opinions in this appeal and in *In re Quanta Resources Corp.* (*City of New York and State of New York* v. *Quanta Resources Corp.*), No. 83-5142 (3rd Cir. July 20, 1984). Each party will bear its own costs.

ATTEST:

SALLY MRVOS
Clerk

July 25, 1984

Certified as a true copy and issued in lieu of a formal mandate on August 28, 1984.

Test:

M. ELIZABETH FERGUSON
Chief Deputy Clerk, United States Court of Appeals for the Third Circuit.

APPENDIX F

Order Denying Petition for Rehearing of the United States Court of Appeals for the Third Crcuit

UNITED STATES COURT OF APPEALS

FOR THE THIRD CIRCUIT

No. 83-5142

IN THE MATTER OF

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

Debtor

THE CITY OF NEW YORK and THE STATE OF NEW YORK

v.

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

State of New York and City of New York

Appellants

No. 83-5730

In Re:

QUANTA RESOURCES CORPORATION

Debtor

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION

Appellant

SUR PETITION FOR REHEARING

PRESENT: ALDISERT, *Chief Judge,* SEITZ, ADAMS, GIBBONS, HUNTER, WEIS, GARTH, HIGGINBOTHAM, SLOVITER and BECKER, *Circuit Judges*

The joint petition for rehearing filed by debtor, Quanta Resources Corporation, and appellee, Thomas J. O'Neill, in the above-entitled case having been submitted to the judges who participated in the decision of this court, and to all the other available circuit judges of the circuit in regular active service, and no judge who concurred in the decision having asked for rehearing, and a majority of the circuit judges of the circuit in regular active service not having voted for rehearing by the court in banc, the petition for rehearing is denied.

Judge Gibbons would grant the petition for rehearing for the reasons set forth in his dissenting opinions.

By the Court

Leonard I. Garth
Circuit Judge

DATED: August 16, 1984

APPENDIX G

Memorandum Opinion of the United States District Court for the District of New Jersey

UNITED STATES DISTRICT COURT

For the District of New Jersey

(B. 81-5967)

Civil No. 82-3524

In the Matter of

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

Debtor.

THE STATE OF NEW YORK and the CITY OF NEW YORK,

Appellants,

v.

THOMAS J. O'NEILL, Trustee in Bankruptcy of Quanta Resources Corp., Debtor,

Appellee.

January 24, 1983

BEFORE:

The Honorable FREDERICK B. LACY, U.S.D.J.

MEMORANDUM OPINION

The Court: This matter is before the court on an appeal from the decision of the Bankruptcy Court which permitted the trustee to abandon property over objections by the City and State of New York.

Quanta Resources ("Quanta") filed a Voluntary Petition in Bankruptcy pursuant to Chapter XI of the Bankruptcy Code. These proceedings were converted to a Chapter VII liquidation, and a trustee was appointed.

The Trustee proposed sale or abandonment of property held by Quanta in Long Island City, New York. Notice was given by the Clerk of the Bankruptcy Court. In response to objections by purported lienholders, a judgment was entered establishing the validity of a lien in the amount of $344,464. No one appeared at the public auction. An offer to purchase the property which was approved by the court was subsequently withdrawn with court approval when the purchaser discovered that hazardous wastes were located at the site.

A second notice was given when the Trustee declared his intention to abandon the property as burdensome to the bankrupt estate. In response to this notice, the State and City of New York objected. They urged that the trustee not be permitted to abandon the property, and that whatever assets existed in the estate should be used to remove the toxic waste from the property. They con-

tended abandonment of the property would violate federal, state and local laws concerning disposal of hazardous waste.

Over these objections, the court ruled that abandonment was permissible under section 554 of the Bankruptcy Code, 11 U.S.C. Sec. 554. The court ruled that the assets in the estate would be distributed to creditors and not be used for purposes of removing the toxic waste. The State and City have since that time expended $2.5 million to remove the toxic waste. They appeal from the Order of the Bankruptcy Court permitting abandonment and seek to have the $2.5 million to remove the toxic waste. They appeal from the Order of the Bankruptcy Court permitting abandonment and seek to have the $2.5 million cost of the cleanup borne by the bankrupt estate.

Section 554(a) of the Bankruptcy Code provides:

> Sec. 554. Abandonment of property of the estate. (a) After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

The parties cannot dispute that the property is burdensome to the estate. Irrespective of the cleanup costs, the liens on the property exceeded the estimated force sale value of the property. Thus, the Trustee was otherwise justified, and by law was required, to seek to abondon the property.

The precise question here is whether abandonment must be denied under 11 U.S.C. Sec. 554 where the abandonment would violate public interest and/or federal, state and local laws. Cases cited by appellants have recog-

nized that abondonment could be denied where the effect of abandonment would be to threaten the public health and safety and/or to violate federal law. See, e.g., Ottenheimer v. Whitaker, 198 F.2d 289 (4th Cir. 1952); In Re Lewis Jones, Inc., 1 B.C.D. 277 (BK. Ct. E.D. Pa. 1974).

In Ottenheimer, the court refused to permit the Trustee to abandon barges because the inevitable sinking of the abandon barges would violate federal law forbidding the obstruction of navigable waterways. The court ordered that the assets of the bankrupt estate be used to remove the barges from the waterway before distribution of assets to creditors. In Lewis Jones, the court refused to permit abondonment of underground utility lines because the untended lines would pose a hazard to health and safety. The court ordered that assets of the estate be used to seal the lines and cement manhole covers before distribution to creditors.

Both Ottenheimer and Lewis Jones were decided before enactment of the Bankruptcy Reform Act of 1978. Therefore, there was no express statutory provision providing for the abandonment of burdensome property. The Lewis Jones court relied, in part, upon section 77(c)(6) of the former Bankruptcy Act, concerning reorganization of railroads, which allowed abandonment only where the public interest would not be harmed thereby. Lewis Jones, supra, 1 B.C.D. at 280. The Ottenheimer court expressed concern that permitting abandonment would subject the trustee or bankrupt to criminal penalties for having obstructed the waterways. Ottenheimer, supra, 198 F.2d at 290. As one commentator has remarked:

> If one of the purposes of the Bankruptcy Act is the rehabilitation of the debtor . . . it seems in-

> consistent to expose him to a criminal proceeding. It may well be that the Trustee himself would be liable for the obstruction of the channel if the barges sink . . . or that he would at least be subject to the penalty for aiding and abetting a violation of the statute by turning the barges over to the bankrupt knowing that they cannot be cared for properly. It would indeed be anamolous for one court to order its officer to do what another could punish as a misdemeanor.

Note, 66 Harv. L. Rev. 921, 922 (1953).

Although the question is a close one, this court concludes the ruling of the Bankruptcy Court must be affirmed. First, both Ottenheimer and Lewis Jones acknowledged that the rules concerning abandonment were judge-made rules which should yield to federal statutes and the general public interest. See, Ottenheimer, supra, 198 F.2d at 290; Lewis Jones, supra, 1 B.C.D. at 280. As the court wrote in Ottenheimer:

> It seems obvious to us that a rule which is not provided by statute but built up by court decisions to facilitate the administration and distribution of assets of a bankrupt estate should not be extended so as to reach such an unreasonable and unjust result. The judge-made rule must give way when it comes into conflict with a statute enacted to ensure the safety of navigation.

Id. at 290.

By contrast, section 554 of the Bankruptcy Code, 11 U.S.C. Sec. 554, constitutes an express statutory provision for the abandonment of burdensome property.

Nowhere is the power to abandon conditioned upon a finding that abondonment does not harm the public interest or violate any statutes. If Congress had intended to place this limitation on the power to abandon, it could have easily done so. Furthermore, as the Lewis Jones court recognized:

> The Supreme Court, in the case of Securities and Exchange Commission vs. United States Realty and Improvement Company, 310 U.S. 434, said that "a bankruptcy court is a court of equity and is guided by equitable doctrines and principles, except as they are inconsistent with the Act. . . ."

Lewis Jones, supra, 1 B.C.D. at 280 (emphasis added). Here, for the Bankruptcy Court to have granted the equitable relief requested and to have compelled that the assets of the bankrupt estate be used to remove the toxic waste would have been inconsistent with section 554 of the Act.

The Bankruptcy Court here ruled:

> The City and State are in a better position in every respect than either the trustee or debtor's creditors to do what needs to be done to protect the public against the dangers posed by the PCB-contaminated facility. But it is not the estate or the debtor's creditors who should finance the requisite cleanup, given the decision of the Trustee to abandon the property.

Transcript of June 22, 1982 Proceedings at 6. The City and the State have failed to demonstrate why the Bankruptcy Court was wrong in deciding that the creditors should not have to pay for the cleanup. The creditors are

not more responsible for the toxic conditions than the general public. And herein lies another problem with compelling that the assets of the estate be used to finance the cleanup.

As noted by the appellants and the Lewis Jones court, abondonment of railroad lines pursuant to the former Act was subject to the requirement that abandonment not violate the public interest. See 11 U.S.C. Sec. 1170(a). However, the legislative history to section 1170 includes the following:

> Subsection (a) permits the court to authorize the abondonment of a railroad line if the abondonment is consistent with the public interest and either in the best interest of the estate or essential to the formulation of a plan . . . The authority to abandon lines of railroad is, of course, subject to the Fifth Amendment to the Constitution, which may in particular cases require abandonment in order not to erode a secured creditor's interest in the debtor's property even though the public interest dictates otherwise.

House Rep. No. 85-595, 95th Cong., 1st Sess. at 423 (1977). This concern was also voiced in In Re New York, New Haven and Hartford Railroad Co., 330 F. Supp. 131, 147 (D. Conn. 1971) where the court wrote:

> The public interest cannot demand the erosion of the bankrupt's assets to the point of confiscating practically the entire asset. At some point, the extent and degree of taking runs into the constitutional prohibition to the Fifth Amendment, the taking of private property for a public use without just compensation.

Here, there is a serious question whether requiring that the estate's assets be used to pay for the cleanup—which would leave nothing for secured creditors—would constitute a taking without just compensation.

Finally, as noted by the Bankruptcy Court, Transcript, supra, at 7, to have refused to permit abandonment would have been "an exercise in futility." Abandonment of the property causes title to vest in the bankrupt who, concededly, does not have sufficient assets to pay for the cleanup. Refusing to permit abandonment would cause the title to remain in the Trustee. But the State and City do not dispute that the Trustee did not, does not, and never will have sufficient assets to finance the cleanup. The Bankruptcy Court expressly weighed this factor in its consideration of the public interest. Id. The court correctly concluded that the public interest would be best served by an expeditious cleanup and that permitting abandonment would result in a quicker cleanup than requiring the Trustee to retain title.

Appellant argued that section 959(b) of the United States Judicial Code, 28 U.S.C. Sec. 959(b), proscribes abandonment. Section 959(b) provides that the Trustee shall "manage and operate" property in his possession according to valid laws However, appellants are unable to cite a case which applied this requirement in a Chapter VII context. According to Professor Moore:

> Sec. 959(b) applies to the Receiver in his operation of property in his possession. It does not apply to the distribution of the estate, and does not require the Federal Receivership Court to comply with state laws regulating distribution of funds in the receivership.

2 Moore's Federal Practice Sec. 66.04(4). For instance, in State of Mo. v. U.S. Bankruptcy Court, 647 F.2d 768, 778 (8th Cir. 1971), the court remarked that a Trustee would not be required to obtain a state license necessary to operate grain warehousing if the Trustee wished to sell grain pursuant to a liquidation of the estate. I find that section 959(b) does not apply to abandonment in a Chapter VII proceeding.

Similarly, the attempted analogy to exception from the automatic stay provisions in cases involving enforcement of state police powers, 11 U.S.C. Sec. 362, is unpersuasive. This is because section 554 does not provide a similar exception to abandonment where the state is seeking to enforce police powers. Furthermore, section 362(a) expressly provides that the exception shall not apply where the governmental unit is pursuing a claim against the property of the debtor. Therefore, reliance of section 362 actually undercuts appellant's argument, inasmuch as the City and State are pursuing a claim against the debtor's property.

The decision of the Bankruptcy Court is affirmed.

APPENDIX H

Order of the United States District Court for the District of New Jersey

(Filed—January 25, 1983)

UNITED STATES DISTRICT COURT

FOR THE DISTRICT OF NEW JERSEY

(B. 81-5967)

Civil No. 82-3524

IN THE MATTER OF

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

Debtor.

THE STATE OF NEW YORK and the CITY OF NEW YORK,

Appellants,

v.

THOMAS J. O'NEILL, Trustee in Bankruptcy of Quanta Resources Corp., Debtor,

Appellee.

Appendix H

This matter having come before the court on an appeal from a decision of the Bankruptcy Court, and a hearing having been held and submissions from the parties having been considered;

IT IS on this 25 day of January, 1983, ORDERED that the decision of the Bankruptcy Court is affirmed, in accordance with a Memorandum Opinion filed with the clerk of the court this date.

FREDERICK B. LACEY
United States District Judge

Appendix H

Docket Entry

CAMDEN - NEWARK - TRENTON
08101 - 07102 - 08605

NEWARK, N. J.

CIVIL NO. 82-3524

IN THE MATTER OF
Quanta Resources Corp., debtor

The State of New York, et al

vs.

Thomas J. O'Neill

There was entered on the docket on 1-26-83 order affirming decision of Bankruptcy court.

ALLYN Z. LITE
CLERK

APPENDIX I

Order Authorizing Abandonment of Property of the United States Bankruptcy Court for the District of New Jersey

(Filed—May 20, 1983)

NOLAN, O'NEILL & MOORE
60 Park Place
Newark, New Jersey 07102
(201) 643-6300
Attorneys for Thomas J. O'Neill, Trustee

UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF NEW JERSEY

Case No. 81-05967

IN RE:

QUANTA RESOURCES CORPORATION,
a corporation of the State of Delaware,

Debtor.

ORDER AUTHORIZING ABANDONMENT OF PROPERTY

This matter having been opened to the Court by Nolan, O'Neill & Moore, attorneys for Thomas J. O'Neilll, Trustee in Bankruptcy of Quanta Resources Corp., debtor, upon a

Notice to Creditors of Proposed Abandonment dated April 23, 1983, and notice having been given to the debtor, its creditors, and other parties in interest of the Trustee's proposed abandonment of the property and of the opportunity to object and request a hearing on such proposed abandonment, and an objection having been filed by the State of New Jersey, Department of Environmental Protection, and the matter coming on to be heard before the Court on May 17, 1983, William F. McEnroe, Esq. of Nolan, O'Neill & Moore, appearing on behalf of the Trustee, Richard F. Engel, Deputy Attorney General, appearing on behalf of the Department of Environmental Protection, and Richard B. Honig, Esq. of Klinger, Honig, Redish & Klinger, appearing on behalf of the landlords, Frola and VonDohlin, and the Court having heard and considered argument of counsel and for good cause shown;

IT IS on this 20th day of May, 1983;

ORDERED that Thomas J. O'Neill, Trustee, be and he is hereby auhtorized to abandon the contents of the tanks located on the premises located at 1 River Road, Edgewater, New Jersey, consisting of mixed industrial and automotive oil, sludge and water, together with any other personal property of the debtor corporation located on said premises and also including any leasehold interest of the Trustee in the premises but reserving to the Trustee possession of that oil which is the subject matter of a sale to Valley Forge Engineering Inc. which oil shall remain in the possession of the Trustee pending completion of the sale, and it is

FURTHER ORDERED that entry of this Order shall be deemed to constitute the abandonment of the aforesaid property by the Trustee effective May 17, 1983, *nunc pro tunc*.

D. JOSEPH DEVITO
United States Bankruptcy Judge

APPENDIX J

Order Authorizing Abandonment of Property of the United States Bankruptcy Court for the District of New Jersey

(Filed—July 7, 1982)

NOLAN, BELL & MOORE
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Newark, New Jersey 07102
Attorneys for Thomas J. O'Neill, Trustee
(201) 643-6300

UNITED STATES BANKRUPTCY COURT

FOR THE DISTRICT OF NEW JERSEY

Case No. 81-05967

IN THE MATTER OF

QUANTA RESOURCES CORP., a corporation of the State of Delaware,

Debtor.

ORDER AUTHORIZING ABANDONMENT OF PROPERTY

This matter having been opened to the Court by Nolan, Bell & Moore, attorneys for Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corp., Debtor, upon

a Notice to Creditors of sale or abandonment of property dated March 18, 1982, and a Notice of Proposed Abandonment dated May 25, 1982, both notices relating to the real and personal property of the debtor corporation located at 37-80 Review Avenue, Long Island City, New York, and notice having been given to the debtor, its creditors and other parties in interest of the Trustees' proposed abandonment of the property and of the opportunity to object and request a hearing on such proposed abandonment, and objections having been filed by the State of New York and by the City of New York, and the matter coming on to be heard before the Court on June 8, 1982, and June 22, 1982, William F. McEnroe, Esq. of Nolan, Bell & Moore appearing on behalf of the Trustee, Norman Spiegel, Esq. and Nancy Stearns, Esq., assistant attorneys generals appearing on behalf of the State of New York, and Gary R. Tarnoff, Esq., assistant corporation counsel, appearing on behalf of the City of New York, and the Court having announced its decision in an oral opinion on June 22, 1982, the terms of which are incorporated herein, and for good cause shown;

IT IS on this 7th day of July, 1982

ORDERED that Thomas J. ONeill, Trustee, be and he is hereby authorized to abandon the real and personal property of the debtor corporation located at 37-80 Review Avenue, Long Island City, New York, and, it is;

FURTHER ORDERED that entry of this Order shall be deemed to constitute the abandonment of said property by the Trustee, effective June 22, 1982, *nunc pro tunc*, and it is;

FURTHER ORDERED that the application by the State of New York to declare a first lien on the subject property

in favor of the State of New York for any moneys expended by the State or City of New York to bring the facility into compliance with New York law and legally dispose of the wastes be and the same is hereby denied.

D. Joseph DeVito
United States Bankruptcy Judge

APPENDIX K

Oral Decision of the United States Bankruptcy Court for the District of New Jersey

UNITED STATES BANKRUPTCY COURT

For the District of New Jersey

Case No. 81-05967

In the Matter of

QUANTA RESOURCES,

Debtor.

TRANSCRIPT OF PROCEEDINGS

BEFORE:

THE HONORABLE D. JOSEPH DE VITO, United States Bankruptcy Court Judge, in Courtroom 6, Federal Courthouse and Post Office Building, Newark, New Jersey, on June 22, 1982, at 2:00 P.M.

1. Ajourned hearing objection to abandonment of Long Island City property by State of New York.

2. Adjourned hearing by trustee on objection to private sale to total recovery.

APPEARANCES:

Messrs. Nolan, Bell & Moore
By: William McEnroe, Esq.
Attorney for Tim O'Neill, Esq., Trustee

Frederick A. O. Schwarz, Jr., Esq.
By: Gary R. Tarnoff, Esq.
Corporation Counsel of the City of New York

Nancy Stearns, Esq.
Norman Spiegel, Esq.
New York Department of Law

Essex-Union Reporting Service
161 Eagle Rock Avenue
Roseland, New Jersey 07068
(201) 228-3118

The Court: I have heard enough gentlemen. The Trustee in this matter has filed a Notice of Intention to abandon real and personal property located at 37-80 Review Avenue, Long Island City, New York, which property has been used for many years as a waste oil processing and storage facility improved with fuel storage tanks containing at present in excess of 500,000 gallons of waste oil and other chemicals of which at least 70,000 gallons of waste oil are contaminated with PCB's. It is undisputed that such equity as may exist in subject property over and above the amount of two mortgage liens would be rapidly dissipated by the costs of necessary and substantial repair and clean-up operations on the facility It appears to the Court, that there is little question if any that the subject

property is burdensome to the estate and of inconsequential or no value to the estate.

The State of New York by its Attorney General, Robert Abrams, joined by the City of New York by its corporation counsel, F. Schwarz, objects to the proposed abandonment. The attorney general points out that to abandon such a facility would be an open invitation to vandals and arsonists. The destruction that they may cause together with the progressive physical deterioration of the facility makes it only a matter of time, the attorney general contends, before the toxic pollutants are discharged into the environment of New York City, threatening public health and safety. The attorney general cites 28 U.S.C. 959 (b), which provides "Except as provided in Section 1166 of Title 11, a Trustee, Receiver or manager appointed in any cause pending in any Court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such Trustee, Receiver or Manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

The attorney general requests that the Trustee not be permitted to abandon the Long Island City facility unless and until the Trustee removes all hazardous wastes from the facility and disposes of those wastes in accordance with New York State and Local Law.

Bankruptcy Code 554 (a), made applicable to liquidation cases under Chapter 7 by Bankruptcy Code 103 (a), permits the Trustee, after notice and a hearing, to abandon any property of the estate that is of inconsequential value or burdensome to the estate.

Upon review of both the fair market and forced liquidation valuation of the facility, the attendant costs associated with its upkeep including twenty-four guard service for the property at a cost exceeding $1,100 per week paid by the Trustee, and the apparently gargantuan task of repair and clean-up, requiring a substantial expenditure, none of which data is materially controverted by the objecting parties, the Court agrees that, by any standard, the subject facility is of inconsequential value and burdensome to the estate.

This case or proceeding was originally filed as a Chapter 11 on October 6, 1981, was converted to a case under Chapter 7 on November 12th, 1981, and on November the 18th, 1981, Thomas O'Neill was appointed Trustee and continues to hold that office.

The violations of State and Local law complained of by the attorney general are not the doing of the Trustee, and the costs of repair of the physical premises and cure of the unquestioned hazardous waste conditions cannot be charged to the bankrupt estate.

It is the duty as well as the right of a Trustee or debtor in possession to seek the Court's approval to abandon property of inconsequential value or burdensome to the estate just as it is the right and duty of the Trustee or debtor in possession to seek the Court's approval for rejection of an executory contract when such contract is burdensome to the estate. And I refer to *in re*: *Investor's Development* 7 B.R. 772, at page 774 and 6 Bankruptcy Court decision, 1415 (Bankruptcy District of New Jersey 1980).

Section 959 of the Judicial Code is not controlling here. The costs of clean-up, maintenance and repair required

to cure the hazardous waste conditions apparently endemic in the property have been factored into the Trustee's calculations whether or not to abandon the property and the Trustee has elected through the power vested in him by Section 554 of the Code to abandon in order both to conserve the assets of and insure the orderly administration and liquidation of the bankrupt estate.

For this Court to grant the relief sought by the attorney general, the right of the Trustee to abandon property of the estate pursuant to Section 554 would be rendered a nullity, as the estate would be made to suffer the resultant costs of managing and operating the property notwithstanding the decision of the Trustee to abandon same.

The City and State of New York are the proper parties to safeguard the health and safety of their citizens. The duty of the Trustee is to serve as representative of the estate, and the duty of this Court is to protect the assets of the estate in custodia legis.

The City and State are in a better position in every respect than either the Trustee or debtor's creditors to do what needs to be done to protect the public against the dangers posed by the PCB-contaminated facility. But it is not the estate or debtor's creditors who should finance the requisite clean-up, given the decision of the Trustee to abandon the property.

Abandonment constitutes a divestiture on the part of the Trustee of all interests in property that were property of the estate. I refer to Collier on Bankruptcy Section 554.02 at 554-8. (15th Edition, 1982), causing possession to revest in the debtor or other party with a possessory interest in the abandoned property.

The Court will, accordingly approve the decision of the Trustee to abandon the property. The request of the attorney general for a first lien on the property so as to prevent an alleged unjust enrichment by the first and second mortgagees, is rejected as unauthorized by the Code.

In reaching the decision, the Court has been very cognizant, mindful and concerned for the public interest in this situation. But I think for this Court to grant the relief requested by the attorney general, would do little else than to put into play an exercise in futility. And would possibly delay the parties who could be chargeable with the clean-up of the property or who have other interest to permit them to move in. That should go forth as quickly as possible. And I think this determination will work in that direction.

Thank you very much.

Mr. Spiegel: May we have a stay of the abandonment so that we can appeal this determination?

The Court: Do you want to be heard Mr. McEnroe?

Mr. McEnroe: We would oppose any stay, anything that would require us to do anything. We have already terminated security. And as you said, it doesn't serve any purpose to stay it.

The Court: I don't know what purpose a stay would be really here where we are abandoning the property. It is going back to the defunct corporation and possibly to the mortgagees.

Mr. Spiegel: We don't know. I certainly don't know what action the defunct corporation might take on the mortgagees in this interval and to maintain this status quo and maintain the jurisdiction of the Court.

The Court: If you are requesting a stay pending an appeal, is that what you are requesting?

Mr. Spiegel: Yes.

The Court: I am afraid, that I must deny the stay. I don't think that that denial affects your interest in anyway.

Mr. Spiegel: Thank you your Honor.

The Court: I don't think there is going to be any movement in this property for some time. The automatic stay continues. There's been no support for the vacating of that stay either before this matter or now.

Thank you very much.

APPENDIX L

Constitutional Provisions and Relevant Statutes

Amendment V—Capital crimes; double jeopardy; self-incrimination; due process; just comsation for property.

No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or navel forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offense to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation

Article VI—Debts validated. Supreme law of land.

All Debts contracted and Engagements entered into, before the Adoption of this Constitution, shall be as valid against the United States under this Constitution, as under the Confederation.

This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution or Laws of any State to the Contrary notwithstanding.

The Senators and Representatives before mentioned, and the Members of the several State Legislatures, and

all executive and judicial Officers, both of the United States and of the several States, shall be bound by Oath or Affirmation to support this Constitution; but no religious Test shall ever be required as a Qualification to any Office or public Trust under the United States.

28 U.S.C.

§ 959. Trustees and receivers suable; management; State laws.

[*See main volume for text of* (*a*)]

(b) Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

(As amended Nov. 6, 1978, Pub.L. 95-598, Title II § 235, 92 Stat. 2667.)

Section 362 (11 U.S.C. § 362)

§ 362 Automatic stay.

(b) The filing of a petition under section 301, 302, or 303 of this title, or of an application under section 5(a)(3) of the Securities Investor Protection Act of 1970 (15 U.S.C. 78eee(a)(3), does not operate as a stay—

(4) under subsection (a)(1) of this section, of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;

(5) under subsection (a)(2) of this section, of the enforcement of a judgment, other than a money judgment, obtained in an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power;

Section 554 (11 U.S.C. § 554)

§ 554 Abandoment of property of the estate.

(a) After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

Section 704 (11 U.S.C. § 704)

§ 704 Duties of trustee. The trustee shall—

(1) collect and reduce to money the property of the estate for which such trustee serves, and close up such estate as expeditiously as is compatible with the best interests of parties in interest;

(2) be accountable for all property received;

(3) investigate the financial affairs of the debtor;

(4) if a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper;

(5) if advisable, oppose the discharge of the debtor;

(6) unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest;

(7) if the business of the debtor is authorized to be operated, file with the court and with any governmental unit charged with responsibility for collection or determination of any tax arising out of such operation, periodic reports and summaries of the operation of such business, including a statement of receipts and disbursements, and such other information as the court requires; and

(8) make a final report and file a final account of the administration of the estate with the court.

No. 84-805

IN THE

Supreme Court of the United States

October Term, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK,
Respondents.

RESPONDENTS' BRIEF IN OPPOSITION

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Assistant Attorneys General
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Assistant Corporation Counsel
Of Counsel

Questions Presented

1. Whether the court below was correct that Congress did not intend the Bankruptcy Code, 11 U.S.C. § 554(a), which authorizes the abandonment of burdensome property, to abrogate federal, state and local laws governing the disposal of hazardous wastes.

2. Whether a trustee can abandon a hazardous waste facility in contravention of state laws and his obligations under 28 U.S.C. § 959(b) to manage and operate the property according to the requirements of valid state laws.

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No. 84-805

IN THE

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THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK,

Respondents.

RESPONDENTS' BRIEF IN OPPOSITION

ARGUMENT

A. A trustee's right to abandon burdensome property pursuant to 11 U.S.C. § 554(a) is subject to the application of a state's police power regulations.

The trustee sought to abandon, as worthless and burdensome, a waste oil processing and storage facility which contained a substantial quantity of hazardous wastes including polychlorinated biphenyls (PCB's) and flammable liquids.

Section 554(a) of the Bankruptcy Code, 11 U.S.C. § 554 (a), permits a trustee to abandon property of the estate which is burdensome or of inconsequential value to the estate. New York, pursuant to its police powers, regulates the handling, storage and disposal of hazardous waste and prohibits its abandonment.[1]

The question presented to the Court of Appeals was whether Congress intended the trustee's abandonment power under federal law to be unrestricted by public health and safety protections embodied in state law—or, to put it plainly, whether a trustee in bankruptcy can ignore state environmental laws concerning hazardous waste.

After a lengthy review of the bankruptcy laws and the authorities interpreting them, the Court of Appeals concluded that there was in fact no indication of any intent on Congress' part to preempt the states' police powers with the enactment of Section 554(a). In reaching this conclusion, the court reasoned that Section 554(a) was merely a codification of a judge-made rule, without any legislative history or limiting language from which an inference could be drawn as to the trustee's authority to supercede the state's police powers. (Pet. App. A pp. 9a, 15a.)

Moreover, the Court noted that construction of Section 554(a) in a manner which does not require the preemption

1. The New York State Environmental Conservation Law, Section 27-0914 and regulations promulgated thereunder at 6 NYCRR 366.4(e), prohibit the disposal of hazardous wastes contrary to the requirements of state statutes and regulations.
The New York City Administration Code, C19-50 *et seq.* requires the maintenance of an operational fire suppression system and round-the-clock supervision by certified personnel at the facility the trustee sought to abandon.

of states' police powers is consistent with established general principles, holding that:

> where important state laws or general equitable principles protect some public interest, they should not be overridden by federal legislation unless they are inconsistent with explicit congressional intent such that the supremacy clause mandates their supersession by the abandonment power. (Pet. App. A p. 14a.)

It also observed that the bankruptcy scheme, viewed in its entirety, contained clear indications that Congress did not intend the Bankruptcy Code to abrogate the enforcement of state police power regulations. (Pet. App. A pp. 15a and 16a.)

Likewise, the Court of Appeals correctly rejected the trustee's claim that abandonment did not violate the state's hazardous waste laws. Abandonment, the trustee had argued, was merely a ministerial act which divested the trustee of title to the property and revested it in the debtor corporation. (Pet. pp. 15-16.) The Court of Appeals recognized that in reality such an act, which separates hazardous waste from the assets needed to check its destructive potential, was a final disposal of the waste which "clearly contravened applicable law, and did so not merely technically but with severely deleterious implications for the public safety." (Pet. App. A p. 21a.)

B. The decision of the Court of Appeals is not contrary to this Court's rule of construction announced in *NLRB v. Bildisco & Bildisco*, 104 S.Ct. 1188 (1984).

The trustee also advances the argument that the decision of the Court of Appeals is contrary to this Court's rule of construction set forth in *NLRB* v. *Bildisco &*

Bildisco, 104 S.Ct. 1188 (1984). *Bildisco*, however, is not inconsistent with the determination of the Court of Appeals in this matter. *Bildisco* held that the term "executory contract," as used in the Bankruptcy Code, 11 U.S.C. § 365(a), did not exclude collective bargaining agreements.[2] This Court observed that although Section 365(a) contained a number of limitations on the power to reject executory contracts, there was no limitation on rejecting a collective bargaining agreement. *Id.*, 104 S.Ct. at 1194. According to the Court, this "statutory design," when viewed in contrast with another section of the Bankruptcy Code, 11 U.S.C. § 1167, which expressly exempted collective bargaining agreements under the Railway Labor Act from the provisions of Section 365(a), showed that Congress did not intend to exempt collective bargaining agreements under the National Labor Relations Act. *Id.*, 104 S.Ct. at 1194-1195.

The trustee's analogy to *Bildisco* would be more compelling if Section 554(a) contained some comparable limitation on the power to abandon burdensome property, for example, proscribing the trustee's abandonment of radioactive materials and biological agents but making no mention of hazardous waste, or explicitly subjecting the trustee's power to abandon to certain enumerated federal or state statutory schemes but making no reference to the state's public health and safety regulations. That, however, is not the case here.

As shown above, Section 554(a) is merely a codification of a judge-made rule, which comes without any legislative

2. Section 365(a) of the Bankruptcy Code, 11 U.S.C. § 365(a), permits a trustee, with the court's approval, to assume or reject any executory contract of the debtor.

history and without any indication that Congress intended to preempt so fundamental a power as the states' police regulations. What is more, as the court below observed, "if trustees in bankruptcy are permitted to dispose of hazardous wastes under the cloak of the abandonment power, compliance with environmental protection laws will be transformed into governmental cleanup by default." (Pet. App. A p. 22a.) The Court of Appeals properly refused to infer "such a radical change in the nature of local public health and safety regulations—the substitution of governmental action for citizen compliance without an indication that Congress so intended." (Pet. App. A p. 22a.)

C. The construction of Section 554(a) of the Bankruptcy Code advanced by the Court of Appeals does not violate the "takings" clause of the Fifth Amendment.

The Court of Appeals correctly rejected the trustee's argument that compliance with the state's police power regulations would result in an unconstitutional taking of property without just compensation. The court's reasoning in this regard is that

> . . . the state's enforcement of its environmental protection laws cannot be characterized as a taking; rather it is a permissible exercise of the state's regulatory power to promote the public good, under a long line of cases dealing with just that distinction. (Pet. App. A p. 23a, note 11.)

Petitioner's reliance on *United States* v. *Security Industrial Bank*, 459 U.S. 70 (1982), to the contrary is misplaced. In *United States* v. *Security Industrial Bank*, the Supreme

Court reviewed a ruling, by the Tenth Circuit Court of Appeals which declared Section 552(f) of the Bankruptcy Code unconstitutional on the grounds that it retroactively extinguished a lienhold interest in violation of the Fifth Amendment. In reversing this decision, the Supreme Court held that there had been no need for the court below to reach the constitutional issue because a review of Section 552(f) did not reveal any congressional intent that it apply retroactively. In so ruling this Court reiterated the well-established principle directing that courts "first ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided." *Id.* 459 U.S. at 78. The trustee distorted this principle of construing statutes to avoid constitutional infirmities into a rule that would compel a finding that Congress intended to preempt the states' police powers, even where no such intent was evident. There is, of course, no such rule of judicial legerdemain.

D. The court below was correct in its construction of 28 U.S.C. § 959(b).

The obligations of a trustee in bankruptcy are governed by the Judicial Code as well as by the Bankruptcy Code. 28 U.S.C. § 959(b) requires the trustee to carry out his duties in compliance with state law, stating:

> Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession shall manage and operate the property in his possession as such trustee, receiver or manager *according to the requirements of the valid laws of the State* in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof. 28 U.S.C. § 959(a) (emphasis added).

The court below concluded that

> . . . although [Section 959(b)] is not itself an independent prohibition of the trustee's abandoning property in contravention of state law, it is a clear indication that in general the congressional scheme was not intended to subjugate state and local regulatory laws. (Pet. App. A p. 17a.)

The court correctly rejected petitioner's argument that Section 959(b) governs the trustee's duties only in a reorganization under Chapter 11 rather than a dissolution under Chapter 7. Petitioner's reliance on a brief statement in 2 Moore's *Federal Practice* 66.04[4], was found to be misplaced. The Court of Appeals agreed with Professor Moore's position that state laws regulating distribution of assets must give way to federal bankruptcy laws, but declared, "[i]t does not follow that state police power regulations must also give way." (Pet. App. A p. 18a.)

There are no Court of Appeals decisions which conflict with the interpretation of Section 959(b) by the Third Circuit. In fact, respondents have found no other decisions which interpret Section 959(b) in the context of liquidation as opposed to reorganization. The interpretation of the court below is, of course, consistent with others in the context of reorganization. *E.g., In Re Chicago Rapid Transit Co.,* 129 F.2d 1 (7th Cir.), *cert. denied,* 317 U.S. 683 (1942); *Gillis* v. *California,* 293 U.S. 62 (1934); *In Re Dolly Madison Industries,* 504 F.2d 499 (3rd Cir. 1974); *In the Matter of Canarico Quarries Inc.,* 466 F. Supp. 1333 (D.P.R. 1979). Thus, there is no need to examine the ruling of the court below.

E. The decision of the court below is consistent with the objectives of the Bankruptcy Code.

Petitioner incorrectly suggests that the opinion of the court below has created a new category of preferences not recognized in the Bankruptcy Code. Rather, the court below concluded that a trustee could not abandon a burdensome asset if the abandonment would violate a state law protecting public health and safety. New York was not arguing for a preferred status as a creditor and the court did not create such a category. The question of reimbursement arose only because the Long Island City facility was abandoned pursuant to the order of the Bankruptcy Court below and New York was compelled to spend its own funds to clean up the abandoned site. This litigation does not involve any claims which might have been owing to New York prior to the abandonment. With respect to such claims, New York would, of course, be an ordinary creditor. In contrast, with respect to clean up costs, New York had no intention of becoming a creditor and acted only because the Bankruptcy Court incorrectly permitted the trustee to abandon the Long Island City facility despite the fact that the abandonment violated federal, state and local laws.

The court below did not in fact reach the question of what, if any, priority New York's expenditures would now have, but rather remanded that question to the Bankruptcy Court. (Pet. App. A p. 25a.) It is therefore premature for this Court to examine that question at this stage of the proceedings.

Finally, petitioner's claim that the ruling of the court below would discourage persons from becoming trustees in bankruptcy is spurious at best. Requiring the assets of

the bankrupt estate to be devoted to cleaning up a hazardous waste site created by or in the possession of the estate should be no more a disincentive to serving as a trustee than any other requirement that there be a distribution of assets among the creditors, as in most liquidations. The court below did not suggest that trustees would be subject to personal sanctions either civilly or criminally because of their responsibility to clean up rather than abandon a hazardous waste site where the estate is the responsible party.[3] The fact that the assets of the estate might be exhausted by the clean up in no way alters the situation. What is more, even if persons who serve as private trustees were unwilling to take over the administrative responsibilities of a hazardous waste site, the United States trustee could be required to do so. *In Re Charles George Land Reclamation Trust,* 30 B.R. 918, 923 (Bkrtcy. 1983).[4]

Conclusion

There is insufficient justification for granting certiorari in this case.

There are no Courts of Appeals decisions which conflict with the decision of the court below. Contrary to petitioner's assertions, the ruling of the court below does not frustrate the objectives of the bankruptcy law, for Congress

3. Of course the trustee would be subject to sanctions for personal misdeeds as with other bankrupt estates. 28 U.S.C. § 959(a).

4. In that case the bankruptcy petition was dismissed, not because of the unwillingness of persons to serve as trustee, but because the court concluded that particularly in light of the likelihood that the trustee would move to abandon the hazardous waste site, the environmental problems could be better addressed in state court. 30 B.R. at 924.

clearly intended that the Bankruptcy Code be enforced in harmony with the police powers of the states.

It is, therefore, respectfully submitted that this Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit be denied.

Dated: New York, New York
December 18, 1984

Respectfully submitted,

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No. 84-805

In The

Supreme Court of the United States

October Term, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK,
Respondents.

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO A PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

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QUESTIONS PRESENTED

1. Whether the court below was correct that Congress did not intend the Bankruptcy Code, 11 *U.S.C.* § 554 (a), which authorizes the abandonment of burdensome property, to abrogate federal, state and local laws governing the disposal of hazardous wastes.

2. Whether a trustee can abandon a hazardous waste facility in contravention of state laws and his obligations under 28 *U.S.C.* § 959(b) to manage and operate the property according to the requirements of valid state laws.

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In The

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COUNTERSTATEMENT OF THE CASE

These companion cases result from appeals by the New Jersey Department of Environmental Protection (hereafter "NJDEP") and the City and State of New York from orders of the United States Bankruptcy Court for the District of New Jersey allowing the trustee in bankruptcy of Quanta Resources Corporation to abandon waste oil reprocessing facilities in Edgewater, New Jersey, and New York City. The Bankruptcy Court relied on 11

U.S.C. § 554, which governs abandonment of property of the bankrupt's estate.

Quanta Resources Corporation is a Delaware corporation which was formed in March, 1980 to engage in the business of waste oil recovery at several sites in New York and in Edgewater, New Jersey. It owned the land in New York City which was used to reprocess oil, and leased the land in New Jersey from James V. Frola and Albert VonDohlin.

With regard to the New Jersey facility, Quanta had taken it over in July, 1980. It had been used by a previous company which had been granted a temporary operating authorization from the NJDEP, which specifically prohibited acceptance of polychlorinated biphenyls (PCB's), an extremely hazardous substance, at the facility. When Quanta took over the facility a similar restriction was placed in its temporary operating authorization. Quanta accepted waste oil and other liquids at the property and put it in its tanks, where it was reprocessed and sold.

A sampling of waste at the site by NJDEP in June, 1981, revealed that PCB's were present in the liquids in the tanks in excess of the permissible standards in the temporary operating authorization. On July 2, 1981, Quanta agreed, at NJDEP's request, to cease operations at the site. Following the shutdown, NJDEP and Quanta began negotiations regarding the cleanup of the property, but on October 6, 1981, Quanta filed for reorganization under Chapter 11 of the Bankruptcy code. On October 7, 1981, NJDEP issued an Administrative Order to Quanta requiring that it cease operations and clean up all hazardous materials at the site. On November 12, 1981, without

the work having been performed as ordered, Quanta filed for conversion of the proceeding in the Bankruptcy Court to a liquidation under 11 *U.S.C.* § 701 *et seq.*

The New Jersey facility, at the time of bankruptcy filing, included tanks holding approximately 3.5 to 5 million gallons of oil, oil sludge, and other liquids. About 400,000 gallons of this oil and sludge contained PCB's in excess of the permissible standard. Approximately 650,000 gallons of the oil that was on the site was able to be sold, and was sold after the bankruptcy filing. The proceeds from the sale were placed in an escrow account. To date, the other liquids remain on the site.

On May 20, 1983, an order was entered by the Bankruptcy Court authorizing the abandonment of the New Jersey property, effective May 17, 1983 *nunc pro tunc* (Pet. App. 64a to 65a).

On September 21, 1983, NJDEP filed a Notice of Appeal by Agreement to the Court of Appeals under 28 *U.S.C.* § 1293(b).

With regard to the New York property, it is located in the geographical heart of New York City, in Queens, and contained approximately 500,000 gallons of waste oil, sludge and hazardous waste on the property, more than 70,000 gallons of which were contaminated with PCB's. The facility was in a state of extreme disrepair.

The facility was operating in New York pursuant to a consent order with the New York State Department of Environmental Conservation (hereafter "NYSDEC"), which obligated Quanta to bring the facility into compliance with New York law. It has been the position of New York throughout these proceedings that the condition of

the facility violated not only the consent order but numerous provisions of the New York State Environmental Conservation Law.

It has been conceded by all parties that the cost of cleanup of the facility exceeded the value of any assets of the property, and in fact, after the bankruptcy was filed the City and State undertook a cleanup which cost approximately $2.5 million.

Following the proper notice, on June 22, 1982, the Bankruptcy Court authorized the Trustee to abandon the property (Pet. App. 69a to 75a). An appropriate order was entered on July 7, 1982, effective June 22, 1982 *nunc pro tunc* (Pet. App. 66a to 68a).

Notice of Appeal to the District Court was filed on July 16, 1982. In an oral opinion on January 24, 1983, and in a subsequent memorandum opinion (Pet. App. 52a to 60a), the District Court affirmed the decision of the Bankruptcy Court. A subsequent appeal was taken to the United States Court of Appeals for the Third Circuit.

Opinions in both the New Jersey and New York cases were filed on July 20, 1984, reversing the decisions of the Bankruptcy and District Courts. (Pet. App. 1a to 48a). The Trustee filed a petition for rehearing in both matters, and on August 16, 1984, rehearing was denied (Pet. App. 49a to 51a).

ARGUMENT

A. The Decision Of The Court Of Appeals Is Not Contrary To Any Of This Court's Prior Rulings.

Petitioner contends that the decision of the Court of Appeals is in conflict with this Court's decision in *NLRB v. Bildisco & Bildisco, — U.S. —*, 104 *S.Ct.* 1188, 79 *L.Ed.* 2d 482 (1984) and *United States v. Security Industrial Bank,* 459 *U.S.* 70, 103 *S.Ct.* 407, 74 *L.Ed.*2d 235 (1982), and therefore this Court should grant the writ of *certiorari* in this case. Respondent, NJDEP, submits that the decision of the Court of Appeals is consistent with both of those opinions, and therefore, *certiorari* should not be granted.

In *Bildisco* this Court was called upon to decide whether the term "executory contract" as used in 11 *U.S.C.* § 365(a) included collective bargaining agreements. A labor union had contended that § 365(a), which permits a trustee to assume or reject any executory contract of a debtor, did not extend to the right to reject a collective bargaining agreement.

In interpreting the meaning of § 365(a), this Court noted that that section contained a number of limitations on the right of a debtor to reject executory contracts, but that there was no limitation regarding the rejection of a collective bargaining agreement. *Bildisco,* 104 *S.Ct.* at 1194. This Court also noted that 11 *U.S.C.* § 1167 expressly exempted collective bargaining agreements under the Railway Labor Act from the provisions of § 365(a), and thus this Court felt that Congress did not intend to exempt collective bargaining agreements made under the

National Labor Relations Act. This Court reasoned that Congress had made a number of exceptions to the right to reject executory contracts, and since collective bargaining agreements was not among them Congress must have intended that they be allowed to be rejected.

Petitioner contends that this reasoning should be used to find that Congress intended, in enacting 11 *U.S.C.* § 554, to allow no exceptions to abandonment, despite the fact that such abandonment may constitute an illegal act according to State law.

There is no inconsistency between the *Bildisco* decision and the decision of the Court of Appeals in this matter. The Court of Appeals held that, with regard to § 554, Congressional intent regarding exceptions cannot be ascertained from a reading of the statute. The entire Bankruptcy Code and other statutes had to also be examined. The Court concluded Congress did not intend an unlimited right to abandon.

This is consistent with *Bildisco*. If § 554 had limited the power to abandon in some instances but not others, the petitioner's argument might be valid. However, it did not. The two decisions are thus not in conflict and provide no reason for this court to grant the writ of *certiorari.*

This Court's decision in *United States v. Security Industrial Bank,* 459 *U.S.* 70, 103 *S.Ct.* 407, 74 *L.Ed.*2d 235 (1982), is also not in conflict with the decision of the Court of Appeals. *Security Industrial Bank* simply stated the well-known principle of construction that constitutional questions should not be addressed if there is another way to interpret a statute to avoid the need to reach those questions. In *Security Industrial Bank* the court

was faced with the question of whether 11 *U.S.C.* § 552(f) should be applied retroactively. This Court held that, since there was no intent on the part of Congress to apply that section retroactively, there was clearly no constitutional taking question that need be decided if retroactivity were found to apply.

Here, however, there is no legislative history or other clear evidence of Congressional intent regarding § 554 of the Bankruptcy Code. Petitioner has raised the taking question, and thus has raised an issue which respondent contends need not be reached for the following reason.

It is not clear from the record whether the inability of the trustee to abandon the property will deplete the assets of the estate or the assets of any creditor. As the Court of Appeals noted, "the trustee argues that use of the estate's assets to comply with State law *may* deplete the estate . . ." (emphasis added). Failure to abandon has no effect on any particular creditor, since secured creditors still have the right to seek relief from the automatic stay and foreclose on their collateral, 11 *U.S.C.* § 362(d), and all other creditors will be in the same position they always were before any attempt to abandon. The court below did not even reach the question of what priority any government expenditures would have in the distribution of the estate. It specifically remanded that question to the Bankruptcy Court (Pet. App. 25a).

Therefore, contrary to petitioner's assertion, this Court would be applying the principle of *Security Industrial Bank,* to avoid unneeded constitutional questions, by not taking this case and allowing the remand to proceed in the Bankruptcy Court.

This Court's recent opinion in *Ohio v. Kovacs,* (No. 83-1020, January 9, 1985) is also not in conflict with the decision of the Third Circuit. *Kovacs* concerned itself with whether a debtor's obligation under a State injunction was dischargable because it was a "debt" or "liability on a claim." This Court held that it was. Respondent NJDEP is not seeking an injunction here, and there is no dispute in this case regarding whether NJDEP has a claim.

This Court also specifically noted that it was not deciding what the duties are of a trustee in bankruptcy, other than that the trustee must comply with state environmental laws while in possession of the site. *Kovacs,* Slip Opinion at 10-11. It was noted that were Kovacs' property in the possession of a trustee in bankruptcy, and were it worth less than the cost of cleanup, the trustee would likely abandon the property. *Kovacs,* Slip Opinion at 10, n. 12. However, this Court did not state whether such conduct by a trustee, if it were in violation of state law, would be permissible under the Bankruptcy Code, and thus the *Kovacs* opinion is not in conflict with that of the Third Circuit.

B. The Question Of The Correctness Of The Court Of Appeal's Interpretation of 11 U.S.C. § 959(b) Need Not Be Reached By This Court.

The Court of Appeals correctly construed 28 *U.S.C.* § 959(b), and its construction is consistent with the prior decisions of other federal courts on this issue. Respondent knows of no other Court of Appeals decisions which conflict with the interpretation of § 959(b) by the Third Circuit, since respondent knows of no other decisions interpreting this section in the context of liquidation. However,

the interpretation is consistent with other opinions in the context of reorganization. *See e.g., Gillis v. California,* 293 *U.S.* 62 (1934); *In the Matter of Canarico Quarries, Inc.,* 466 *F.Supp.* 1333 (D.P.R. 1979); *In re Dolly Madison Industries,* 504 *F.*2d 499 (3rd Cir. 1974); *In re Chicago Rapid Transit Company,* 129 *F.*2d 1 (7th Cir.), *cert.* den., 317 *U.S.* 683 (1942).

This Court also recently noted in *Ohio v. Kovacs* (83-1020, January 9, 1985), that any person in possession of a site that is part of a bankrupt estate, whether it is a receiver or a trustee in bankruptcy, must comply with environmental laws. Slip Opinion at 10-11. This is consistent with the holding of the Third Circuit below.

However, this Court need not reach the question of the interpretation of 28 *U.S.C.* § 959(b), because the Court of Appeals only discussed the section as an example of why it felt that Congressional intent, as embodied in § 554 of the Bankruptcy Code, prohibited abandonment of property when such abandonment would contravene state and local health laws. As an indication that Congress did not intend the abandonment power to be absolute, the court noted that 28 *U.S.C.* § 959(b) requires a trustee in bankruptcy to comply with state law.

C. This Court Need Not Decide Whether Abandonment In This Case Violates State Laws Or Regulations.

Petitioner asserts that the court below erred in deciding that abandonment would contravene New Jersey and New York laws, and therefore this Court should accept this case to reverse that holding. However, such a decision by the court below is not: a) in conflict with deci-

sions of other Circuits of Court of Appeals; b) an important question of federal law; or c) in conflict with any prior decisions of this Court.

Rather, all of the lower courts in this matter based their decisions on the assumption that abandonment would, in and of itself, violate the requirements of New York and New Jersey law (Pet. App. 6a, 54a, 72a). Each of the 50 states has different laws with regard to environmental protection. Therefore, for this Court to decide that the lower courts were incorrect in their assertions regarding the meaning of New York and New Jersey laws would not help the federal courts in the other 48 states when faced with the issue of the interpretation of § 554 of the Bankruptcy Code. The petition for writ of *certiorari* should therefore be denied.

D. The Decision Of The Court Of Appeals Will Not Frustrate The Objectives Of The Bankruptcy Code.

Petitioner asserts that the purposes of the Bankruptcy Code would be frustrated by the application of the decision of the court below. (See Petitioner's Brief at p. 18 to 27). Petitioner's assertion is based on his belief that the opinion of the court below assigned a priority to the claims of New York and New Jersey. On the contrary, however, the court below specifically declined to set such a priority.

New York had asked that its cost of cleanup be reimbursed out of the estate as an "administrative expense" as defined in 11 *U.S.C.* § 503(b) and § 507(a). The court held that,

> we need not, however, reach the issue of the priority, if any, of New York's claim. That is an issue that can properly be resolved only by the Bankruptcy Court, since the issue was not treated in the proceedings below and so the record on appeal does not include findings of relevant facts. (Pet. App. at 25a).

All that the court below held was that a trustee may not abandon property when such abandonment contravenes State and local public health laws. Thus, a trustee must retain possession of the property until the liquidation of the estate is complete. In some instances, a trustee may be required to expend assets of the estate during that time to prevent violation of State laws, including environmental protection and health laws. He also may not. States may or may not choose to expend their own funds during that time to correct violations of environmental and health laws. If they do, they may decide to file claims against the estate. The trustee then, with court approval, would be required to deal with these claims as with any other claims, according to the requirements of the Bankruptcy Code. *See* 11 *U.S.C.* §§ 503 and 507. New York and New Jersey have not asserted otherwise in this proceeding.

Respondent thus fails to see how the request that a trustee not abandon property in any way frustrates the purposes of the Bankruptcy Code, which petitioner has defined as the swift reduction of the debtor's property to money and the fair and equitable distribution to the debtor and its creditors of the estate. The court below has not created a preference for New York or New Jersey. It simply directed that the Bankruptcy Court consider what priority New York's claim might have, along with the claims of all other creditors.

With regard to the New Jersey facility, the court specifically noted that "NJDEP . . . has not argued it should be reimbursed for any expenses incurred in cleaning up or restoring the property . . .," and thus did not address that issue (Pet. App. 39a). The court reiterated:

> the issue is not who should pay to clean up the estate's property; it is whether the trustee's interest in preserving the estate should prevail over the public's interest in containing the hazards produced by toxic wastes in the possession of the estate. As in the companion case where the State and City of New York are appealing, we are convinced that the equities must be balanced in favor of the public interest. *Id.*

The petitioner finally asserts that the purposes of the Bankruptcy Code would be frustrated should the decision below stand, because no one would agree to be a trustee in bankruptcy. Again, petitioner misconstrues the opinion of the court below. That decision simply requires that the trustee in bankruptcy follow state and local laws to the extent that the funds in the estate allow. Trustees in bankruptcy are required frequently to balance competing requests for funds while the estate is being liquidated. This decision requires nothing different. In addition, even if a private trustee does not wish to serve, the United States trustee could be required to do so under 11 *U.S.C.* § 15107.

Petitioner also suggests that for some reason trustees would be subject to civil or criminal sanctions because of failure to clean up hazardous wastes that might exist at a site. Such sanctions under 28 *U.S.C.* § 959(b) would only be applied, however, if the trustee, while in possession of the assets of the estate, violates a state or local health or environmental law. This is no different than if the trustee were to violate any other law while he is in possession of the estate.

In summary, nothing in the decision below conflicts with any of the purposes of the Bankruptcy Code.

CONCLUSION

There is no reason why the writ of *certiorari* should be granted in this case. The decision of the Court of Appeals does not conflict with any decisions of other courts of appeals. The decision also does not conflict with any prior decisions of this Court, and the questions presented by the petitioner are not so novel or important questions of interpretation of federal law that they require the granting of this writ.

It is therefore respectfully submitted that this petition for writ of *certiorari* to the United States Court of Appeals for the Third Circuit be denied.

DATED: Trenton, New Jersey
January 16, 1985

Respectfully submitted,

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(3) (4)

Nos. 84-801 and 84-805

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

MIDLANTIC NATIONAL BANK,

Petitioner (No. 84-801),

vs.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,

Respondent,

and

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner (No. 84-805),

vs.

THE CITY OF NEW YORK and STATE OF NEW YORK, *et al.*,

Respondents.

On Writs of Certiorari to the United States Court of Appeals For the Third Circuit

BRIEF OF PETITIONER, MIDLANTIC NATIONAL BANK

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PETITIONS FOR CERTIORARI FILED NOVEMBER 14, 1984

CERTIORARI GRANTED AND CASES CONSOLIDATED
FEBRUARY 19, 1985

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Questions Presented for Review

1. Whether the Third Circuit Court of Appeals erred in holding that a bankruptcy trustee's ability to abandon burdensome and valueless property under 11 U.S.C. §554 is conditioned upon compliance with state environmental regulations?

2. Whether the Third Circuit Court of Appeals erred in interpreting 11 U.S.C. §554 and 28 U.S.C. §959(b) so as to raise a substantial question as to the taking of property without just compensation in sharp conflict with the decision of this Court in *United States* v. *Security Industrial Bank,* 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982)?

Parties

The parties who appeared before the Third Circut Court of Appeals in Case No. 83-5730 are listed below.

The New Jersey Department of Environmental Protection, Appellant.

Thomas J. O'Neill, Trustee for Quanta Resources Corporation, Appellee.

Midlantic National Bank, Appellee.

James V. Frola and Albert Von Dohlin, Appellees.

The parties who appeared before the Third Circuit Court of Appeals in Case No. 83-5142 are listed below.

The City of New York and the State of New York, Appellants.

Thomas J. O'Neill, Trustee for Quanta Resources Corporation, Appellee.

The State of New Jersey, *Amicus Curiae.*

The Commonwealth of Pennsylvania, *Amicus Curiae.*

The Department of Environmental Resources of the Commonwealth of Pennsylvania, *Amicus Curiae.*

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Nos. 84-801 and 84-805

IN THE

Supreme Court of the United States

October Term, 1984

MIDLANTIC NATIONAL BANK,

Petitioner (No. 84-801),

vs.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,

Respondent,

and

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner (No. 84-805),

vs.

THE CITY OF NEW YORK and STATE OF NEW YORK, *et al.*,

Respondents.

On Writs of Certiorari to the United States Court of Appeals For the Third Circuit

BRIEF OF PETITIONER, MIDLANTIC NATIONAL BANK

Opinions and Judgment Below

The opinion of the Third Circuit Court of Appeals in the action involving the New Jersey property, Case No. 83-5730, is reported at 739 F.2d 927 and is set forth at pages 35a to 40a of the appendix to the Petition of Trustee Thomas J. O'Neill ("the Trustee"). The amended judgment of the Court of Appeals in that case is set forth at pages 47a to 48a of the appendix to the Petition filed by the Trustee. The order denying the petition for rehearing by the Circuit Court of Appeals is set forth at pages 49a to 51a of the appendix to the Petition filed by the Trustee. The order of the United States Bankruptcy Court for the District of New Jersey authorizing abandonment of the New Jersey property is set forth at pages 64a to 65a of the appendix to the Petition filed by the Trustee.

The opinion of the Third Circuit Court of Appeals in the companion case of *City of New York* v. *Quanta Resources Corp. (In the Matter of Quanta Resources Corporation, Debtor),* is reported at 739 F.2d 912. This opinion is also set forth at pages 1a to 43a of the appendix to the Petition filed by the Trustee. The opinion of the United States District Court for the District of New Jersey in the companion case is not reported but is set forth at pages 52a to 60a of the appendix to the Petition filed by the Trustee. The opinion of the United States Bankruptcy Court for the District of New Jersey in the companion case is not reported but is set forth at pages 69a to 75a of the appendix to the Petition filed by the Trustee.

Jurisdiction

Midlantic National Bank ("Midlantic") and the Trustee have invoked jurisdiction of the Court under 28 U.S.C. §1254(1). The judgments of the Court of Appeals in Case No. 83-5154 and in Case No. 83-5730 were entered on July 20, 1984. On August 16, 1984, the Court of Appeals denied rehearing.

Constitutional Provisions and Statutes

The Supremacy Clause of Article 6 and the Fifth Amendment to the United States Constitution along with three federal statutes, 11 U.S.C. §554(a), 11 U.S.C. §704, and 28 U.S.C. §959(b), are central to this matter.

Article VI, Clause 2:

> This Constitution, and the Laws of the United States which shall be made in Pursuance thereof; and all Treaties made, or which shall be made, under the Authority of the United States, shall be the supreme Law of the Land; and the Judges in every State shall be bound thereby, any Thing in the Constitution of Laws of any State to the Contrary notwithstanding.

Amendment V:

> No person shall be held to answer for a capital, or otherwise infamous crime, unless on a presentment or indictment of a Grand Jury, except in cases arising in the land or naval forces, or in the Militia, when in actual service in time of War or public danger; nor shall any person be subject for the same offence to be twice put in jeopardy of life or limb; nor shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law; nor shall private property be taken for public use, without just compensation.

11 U.S.C. §554(a):

After notice and a hearing the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

11 U.S.C. §704:

The trustee shall—

(1) collect and reduce to money the property of the estate for which such trustee serves, and close such estate as expeditiously as is compatible with the best interests of parties in interest;

(2) be accountable for all property received;

(3) ensure that the debtor shall perform his intention as specified in section 521(2)(B) of this title;

(4) investigate the financial affiairs of the debtor;

(5) if a purpose would be served, examine proofs of claims and object to the allowance of any claim that is improper;

(6) if advisable, oppose the discharge of the debtor;

(7) unless the court orders otherwise, furnish such information concerning the estate and the estate's administration as is requested by a party in interest;

(8) if the business of the debtor is authorized to be operated, file with the court and with any governmental unit charged with responsibility for collection or determination of any tax arising out of such operation, periodic reports and summaries of the operation of such business, including a statement

of receipts and disbursements, and such other information as the court requires; and

(9) make a final report and file a final account of the administration of the estate with the court.

28 U.S.C. §959(b):

Except as provided in section 1166 of title 11, a trustee, receiver or manager appointed in any cause pending in any court of the United States, including a debtor in possession, shall manage and operate the property in his possession as such trustee, receiver or manager according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

Statement of the Case

These two companion cases, arising out of the same bankruptcy proceeding, present to the Court the question of the construction of the abandonment provision of the Bankruptcy Code, 11 U.S.C. §554, and the interrelationship of that statutory provision with other state and federal laws. The question arises in the context of a bankruptcy liquidation involving a debtor which had conducted waste oil recycling operations in Edgewater, New Jersey, and Long Island City, New York.[1] Abandonment of the two sites by the Trustee is opposed by the environmental agencies of

[1] Insofar as Midlantic's security interest in certain property of the debtor does not extend to the Long Island City facility, Midlantic will rely upon the Trustee to set forth the specific facts concerning abandonment of that facility.

New York and New Jersey who seek to compel the Trustee to bring the sites into compliance with all environmental laws.

Quanta Resources Corporation ("Quanta") was formed as a Delaware corporation in March 1980.[2] In July 1980, Quanta entered in an agreement to acquire Edgewater Terminals, Inc., and its interest in a lease for property located at 1 River Road, Edgewater, New Jersey (R. Stip. ¶6). Through this agreement, a Temporary Operating Authorization ("TOA") from the New Jersey Department of Environmental Protection ("NJDEP") to operate a waste oil recovery business at the Edgewater site was assigned to Quanta (R. Stip. ¶¶4, 7).

With the TOA in hand, Quanta accepted waste oil and oil sludge at the Edgewater property in order to process the oil for resale (R. Stip. ¶7). On June 3, 1981, Quanta borrowed $600,000.00 from Midlantic for working capital and executed a Note and Security Agreement (R. Stip. ¶9). Midlantic's security interest in Quanta's inventory, accounts receivable and several items of equipment was duly perfected pursuant to New Jersey law (R. Stip. ¶9).[3] By Order dated April 5, 1982, the United States Bankruptcy Court for the District of New Jersey determined that Midlantic holds a valid first priority lien in the sum of $643,-

[2] Paragraph 5 of the Stipulation of Facts filed on December 20, 1982, in *Frola* v. *O'Neill* (*In re Quanta Resources Corporation*), Case No. 81-05967, Adversary No. 82-0753 (Bkrtcy. D.N.J.) designated as item seven in the Designation of Contents for Inclusion in Record on Appeal. For ease of reference, subsequent citations will be made according to the following form—R. Stip. ¶5.

[3] Midlantic's security interest did not extend to any of Quanta's Long Island City property.

660.68 in the various item of the debtor's Edgewater property including the waste oil inventory relevant to this application (R. Stip. ¶11).

Late in June 1981, NJDEP sample waste oil stored by Quanta at the Edgewater site and discovered unlawful concentrations of polychlorinated biphenyls ("PCBs") (R. Stip. ¶8). Under the terms of the TOA, PCBs could not be stored at the faciilty (R. Stip. ¶8). As a result, on July 2, 1981, Quanta complied with a NJDEP request and ceased all operations at the Edgewater site (R. Stip. ¶10).

On October 6, 1981, Quanta filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code (R. Stip. ¶1). The Chapter 11 petition was converted to a Chapter 7 liquidation proceeding on November 18, 1981 and on that same day Thomas J. O'Neill was designated as the Quanta trustee (R. Stip. ¶2).

The Trustee proceeded to sell a portion of the waste oil inventory that was not contaminated with PCBs, generating a sum of approximately $288,000.00 (R. Stip. ¶12).[4]

[4] On July 7, 1982, the owners of the Edgewater property, Frola and Von Dohlin, started an action in the Bankruptcy Court seeking, *inter alia,* an order directing the Trustee to turn over the proceeds of the sale of this oil to the landowners. *Frola* v. *O'Neill* (*In re Quanta Resources Corporation*), Case No. 81-05967, Adversary No. 82-0753(Bkrtcy. D.N.J.) NJDEP cross-claimed seeking the funds for future cleanup of the site. By order of April 27, 1983, the Bankruptcy Court dismissed the claim of the landowners and the NJDEP and deferred resolution of Midlantic's turnover application as being premature. The NJDEP appeal to the District Court from this order is now pending although on "administrative hold" until the abandonment issue is resloved. *Frola* v. *O'Neill* (*In re Quanta Resources Corporation*), Civil Action No. 83-4358 (D.N.J.). Pursuant to a consent order, the Trustee has distributed the proceeds to various parties subject to further adjudication of NJDEP's rights.

In addition, through notices issued on October 8, 1982, October 18, 1982, and April 22, 1983, the Trustee announced his intention to abandon the PCB laden waste oil inventory in Edgewater (R. Stip. ¶19; R. October 8, 1982, Notice; R. October 18, 1982, Revised Notice; R. April 22, 1983, Notice). Over NJDEP objections of October 14, 1982, and April 27, 1983, the Bankruptcy Court authorized abandonment of the Edgewater site by order of May 20, 1983[5] (R. May 20, 1983, Order reprinted at Appendix I to the Trustee's Petition for Certiorari).

Since the abandonment issued raised in the New Jersey case was already pending before the Court of Appeals for the Third Circuit, a notice of appeal by agreement to the Court of Appeals under 28 U.S.C. §1293(b) was filed by NJDEP on September 21, 1983 (R. Notice of Appeal). It is important to note that in the appeal NJDEP did not challenge the conclusion of the Bankruptcy Court that the Edgewater facility and its contaminated waste oil inventory were of no value and were instead a great burden to the estate. Instead, NJDEP argued that the Trustee could not abandon the burdensome property because of a duty to clean up the environmental contamination arising under police power laws of the State of New Jersey (R. Statement of Issue on Appeal).

Over the dissent of Circuit Judge Gibbons, the Third Circuit Court of Appeals reversed the decision of the Bankruptcy Court holding that the Trustee would violate state environmental legislation if he were to abandon the contaminated oil and that the Trustee must somehow bring the Edgewater site into compliance with local environmental laws.

[5] The United States Bankruptcy Court for the District of New Jersey had jurisdiction over the abandonment application under §405 of the Bankruptcy Reform Act of 1978, Pub. L. 95-598, Title IV, 92 Stat. 2686 (1978), *reprinted in note preceding*, 28 U.S.C.A. §1471 (West Supp. 1983) and Local Rule 47 of the United States District Court for the District of New Jersey that was issued on October 1, 1982.

Summary of Argument

1. The Court of Appeals violated a canon of statutory construction in interpreting the abandonment provision of the Bankruptcy Code, 11 U.S.C. §554(a), so as to raise a substantial constitutional issue of taking under the Fifth Amendment to the United States Constitution. *United States* v. *Security Industrial Bank,* 459 U.S. 70, 103 S.Ct. 401, 74 L.Ed.2d 235 (1982). The Fifth Amendment commands that the burden of cleaning up environmental problems of a valueless asset abandoned by a trustee in bankruptcy be borne by the general public and not the creditors of the debtor's estate. *Louisville Joint Stock Land Bank* v. *Radford,* 295 U.S. 555, 55 S.Ct. 854, 79 L.Ed. 1593 (1935).

2. Congress did not intend that abandonment of burdensome and valueless assets of an estate being liquidated in bankruptcy be conditioned upon a trustee first spending assets that would otherwise go to creditors so as to bring the abandoned property into compliance with state environmental laws.

(a) Abandonment of a burdensome asset does not constitute an act or omission triggering liability for a trustee under environmental laws. *Brown* v. *O'Keefe,* 300 U.S. 598, 57 S.Ct. 543, 81 L.Ed. 827 (1937).

(b) Public policy demands that trustees serving under federal bankruptcy law not assume personal responsibility

for environmental problems arising through prepetition conduct of debtors.

(c) The Court of Appeals erred in creating a limitation upon a trustee's ability to abandon burdensome estate assets in view of the clear and conclusive language of 11 U.S.C. §554(a). *United States* v. *Clark,* 454 U.S. 555, 102 S.Ct. 895, 70 L.Ed.2d 768 (1982). *Ohio* v. *Kovacs,* —— U.S. ——, 105 S.Ct. 705, 83 L.Ed.2d 649 (1985).

3. Insofar as they impact upon 11 U.S.C. §554(a) and a trustee's ability to abandon burdensome property, state environmental laws stand as an obstacle to the purposes and objectives of Congress and fall under the supremacy clause. *Perez* v. *Campbell,* 402 U.S. 637, 91 S.Ct. 1704, 29 L.Ed.2d 233; *Hines* v. *Davidowitz,* 312 U.S. 52, 61 S.Ct. 399, 85 L.Ed. 581 (1941).

ARGUMENT

POINT I

The interpretation given to 11 U.S.C. §554(a) by the Court of Appeals raises a substantial question under the taking clause of the Fifth Amendment and therefore conflicts with the rule of statutory construction confirmed in *United States* v. *Security Industrial Bank,* 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982).

As a creditor with a perfected security interest in the fund created from the sale of a portion of Quanta's waste oil inventory, Midlantic has raised its voice on its own and on behalf of all creditors against the far reaching interpretation given to 11 U.S.C. §554(a) by the Court of Appeals. Under the decision below, who must bear the huge cost of disposing of the PCB contaminated oil?[6] No party has ever challenged the fact that the Trustee has never had sufficient funds to clean up either site. Nonetheless, the Court of Appeals reversed the Bankruptcy Court orders authorizing abandonment directing that the environmental cleanup costs be evaluated as administrative expenses on remand. *City of New York* v. *Quanta Resources Corp. (In re Quanta Resources Corp.),* 739 F.2d 912, 923 (3d Cir. 1984); *In re Quanta Resources Corporation,* 739 F.2d 927, 929 (3d Cir. 1984).[7] Through this command, the

[6] Following abandonment of the Long Island City property by the Trustee, New York City and New York State cleaned up that site at an expense of approximately $2,500,000.00 (Petition of Trustee, p. 5, footnote 2). To date NJDEP has not taken any action to clean up the Edgewater site.

[7] In his dissent in the New York case, Circuit Judge Gibbons criticized the majority's sidestep of the administrative expense

(Footnote continued on following page)

Court of Appeals has shifted the burden of environment compliance from the debtor to the Trustee to the creditors, possibly including secured creditors such as Midlantic, "who, on the record before us, were in no way responsible for placing the contaminated oil on that site". *Id.* at 925 (dissent of Judge Gibbons).

Midlantic respectfully asserts that the Court of Appeals violated a canon of statutory construction in its drive to advance the important policy of protecting the public health by regulating disposal of toxic wastes. *See, City of New York* v. *Quanta Resources Corp.*, 739 F.2d at 921. Throughout this litigation, both Midlantic and the Trustee have argued that a rule conditioning the clear command of the abandonment provision of the Bankruptcy Code, 11 U.S.C. §554(a), would raise a serious taking issue under the Fifth Amendment. Yet, the Court of Appeals saw no taking question arising under the Fifth Amendment in the destruction of Midlantic's rights as a secured creditor in favor of the public welfare. Indeed, the constitutional argument was dismissed in a footnote. *City of New York* v. *Quanta Resources Corp.*, 739 F.2d at 922 (footnote 11). This casual dismissal of the taking issue completely disregarded the rationale of this Court in *United States* v. *Security Industrial Bank*, 459 U.S. 70, 103 S.Ct. 401, 74 L.Ed.2d 235 (1982).

(Footnote continued from preceding page)

priority issue as irresponsible. *City of New York* v. *Quanta Resources Corp.*, 739 F.2d at 925. Expanding the Third Circuit Quanta opinions, one Bankruptcy Court has recently held that environmental claims are administrative expenses under 11 U.S.C. §503 and are entitled to priority over all unsecured creditors under 11 U.S.C. §507(a)(1). *In re T.P. Long Chemical, Inc.*, 45 B.R. 278, 286-290 (Bkrtcy. N.D. Ohio 1985).

In *Security Industrial Bank*, a secured creditor challenged retrospective application of §522(f)(2) of the Bankruptcy Code, 11 U.S.C. §522(f)(2), as an unconstitutional taking of a pre-enactement lien under the Fifth Amendment. On review, this Court first noted that under *Louisville Joint Stock Land Bank* v. *Radford*, 295 U.S. 555, 55 S.Ct. 854, 79 L.Ed. 1593 (1935) the bankruptcy power is subject to the Fifth Amendment's prohibition against taking private property without compensation. 459 U.S. at 75, 103 S.Ct. at 410, 74 L.Ed.2d at 240. The *Security Industrial Bank* Court next reviewed the nature of the claimed taking and found that the government action would result in a complete destruction of the property right of the secured party. 459 U.S. at 75, 103 S.Ct. at 411, 74 L.Ed. 2d 241. To avoid this grave constitutional question, the Court applied the cardinal principle of statutory construction that a statute should be construed so as to avoid a constitutional question if an alternative interpretation is fairly possible. *Security Industrial Bank*, 459 U.S. at 78, 103 S.Ct. at 412, 74 L.Ed.2d at 243. Stated alternatively:

> As a corollary of the presumption favoring constitutionality, the fact that one among alternative constructions would involve serious constitutional difficulties is reason to reject that interpretation in favor of another.

2A N.J. Singer, *Sutherland Statutory Construction*, §45.11 (Sands 4th Ed. 1984).

As in *Security National Bank*, the interpretation given to 11 U.S.C. §554(a) by the Court of Appeals creates a very serious question of an unconstitutional taking of private property under the Fifth Amendment. Indeed, in footnote eleven of the Long Island City abandonment opinion, the Third Circuit concluded that it would be constitutionally reasonable to require that proceeds normally

targeted for satisfaction of a secured creditor's lien be instead spent by the Trustee to comply with toxic waste disposal. 739 F.2d at 922.[8] The end result would be total destruction of Midlantic's lien since, even including the money that would be otherwise paid to Midlantic, the Trustee only has a small fraction of the funds necessary to compensate the New York regulatory agencies for cleanup of the Long Island City site.

In dismissing the taking issue, the Court of Appeals categorized enforcement of New York and New Jersey environmental laws as a permissible regulatory activity and not an unconstitutional taking. 739 F.2d at 922 (footnote 11). Midlantic respectfully disagrees. Starting with *Village of Euclid* v. *Ambler Realty Co.,* 272 U.S. 365, 47 S.Ct. 114, 71 L.Ed. 303 (1926) (zoning ordinance limiting use of property valid as exercise of police power) through *Agins* v. *City of Tiburon,* 447 U.S. 255, 100 S.Ct. 2138, 65 L.Ed.2d 106 (1980) (zoning ordinance placing land in residential planned development and open space zone), this Court has repeatedly recognized that reasonable regulatory actions do not constitute unlawful takings. However, reasonableness has its limits and at some point in time regulation crosses the line to become confiscation. As noted by Justice Brandeis in the *Louisville Joint Stock Land Bank* v. *Radford* opinion:

> [T]he Fifth Amendment commands that, however great the Nation's need, private property shall not be thus taken even for a wholly public use without just compensation. If the public interest requires, and permits, the taking of property of individual mortgages in order to relieve the necessities of individual mortgagors, resort must be had to proceedings by eminent domain; so that, through taxation, the burden of the relief afforded in the public interest may be borne by the public.

295 U.S. at 602.

Since implementation of the Third Circuit decisions in the two *Quanta* cases will undoubtedly lead to total destruction of Midlantic's property interest, reliance upon the cases upholding limited regulatory activities stands completely off the mark. The result is not regulation but destruction. Moreover, the effect falls upon an innocent third party and not a primary actor somehow responsible for the necessity of the regulatory action. On these facts the Court of Appeals erred in finding that its construction of 11 U.S.C. §554(a) did not raise a substantial question under the taking clause of the Fifth Amendment.

Once such a question was raised, the holding of this Court in *United States* v. *Security Industrial Bank,* 479 U.S. 70, 103 S.Ct. 407, 74 L.Ed. 2d (1982) required that the Court of Appeals ascertain whether another construction of 11 U.S.C. §554(a) would avoid the constitutional question. 459 U.S. at 78, 103 S.Ct. at 412, 74 L.Ed. 2d at 243; *see also, Lorillard* v. *Pons,* 434 U.S. 575, 577, 98 S.Ct. 866, 868 55 L.Ed.2d 40 (1978). A construction that would not condition abandonment upon environmental compliance would certainly avoid the taking issue. Moreover, as demonstrated through Point II of this Brief, any alternative construction would flatly contradict the intention of Congress in enacting §554(a).

[8] This conclusion conflicts with the recent decisions of the Bankruptcy Court for the Northern District of Ohio In *In re T.P. Long Chemical, Inc.,* 45 B.R. 278 (Bkrtcy. N.D. Ohio 1985). Nonetheless, absent reversal by this Court, the New Jersey Bankruptcy Court will probably be persuaded by the reasoning of the Third Circuit on remand.

POINT II

Abandonment of burdensome and worthless property pursuant to 11 U.S.C. §554(a) by a trustee serving in a liquidation proceeding under Chapter 7 of the Bankruptcy Code is not conditioned upon compliance with local police power regulations.

A. The Court of Appeals seriously misconstrued §554(a) of the Bankruptcy Code in holding that a trustee would violate environmental protection laws by abandoning contaminated property.

In the two decisions below, the Court of Appeals held that the Trustee could not abandon burdensome property because abandonment would contravene state and local environmental laws. *City of New York* v. *Quanta Resources Corp.,* 739 F.2d at 913; *In re Quanta Resources Corporation,* 739 F.2d at 928-929. Midlantic asserts that one reason why these holdings are wrong is that the Court of Appeals misconstrued the basic issue on appeal. The true issue being whether abandonment may be conditioned upon compliance with state and local environmental laws instead of whether the Trustee would actually violate such laws upon abandonment. A brief review of the history of a trustee's abandonment power shows why the phrasing of this issue is so important.

Prior to 1978, the law of bankruptcy was governed by the Bankruptcy Act of 1898. The Bankruptcy Act did not contain a specific statutory provision governing abandonment of property in the liquidation context. *See, Ottenheimer* v. *Whitaker,* 198 F.2d 289, 290 (4th Cir. 1952), *affirming,* 102 F. Supp. 103 (D.Md. 1952) and 4 L.P. King, *Collier on Bankruptcy,* ¶554.01 (15th Ed. 1985). Instead, case law permitted a trustee to abandon valueless property so as to further the paramount purpose of liquidation—

the reduction of the debtor's property to money for expeditious distribution to general creditors. 4 L.P. King, *Collier on Bankruptcy,* ¶554.01 (15th Ed. 1985). The common law rule has now been replaced by a specific statutory provision governing abandonment—11 U.S.C. §554(a).

In addition, title to property of the debtor's estate was treated differently under the prior Bankruptcy Act.

> Former section 70a of the Act vested title to the debtor's property in the trustee. Abandonment then divested the trustee of this title and revested it in the debtor. Under Section 541 (11 U.S.C. §541), the Trustee no longer takes title to the debtor's property, and, upon abandonment under Section 554, the trustee is simply divested of control of the property because it is no longer part of the estate. Thus, abandonment constitutes a divesture of all interests in the property that were property of the estate.

4 L.P. King, *Collier on Bankruptcy,* ¶554.02(2) (15th Ed. 1985). However, even under the prior act, title to property abandoned by a trustee revested in the debtor as of the date of commencement of the bankruptcy proceeding. *Brown* v. *O'Keefe,* 300 U.S. 598, 602, 57 S.Ct. 543, 81 L.Ed. 827 (1937). This "legal fiction" continues under applicataion of §554(a). *Mason* v. *C.I.R.,* 646 F.2d 1309, 1310 (9th Cir. 1980); *In re Cruseturner,* 8 B.R. 581, 591-592 (Bkrtcy. D.Utah 1981). The analysis of Bankruptcy Judge Mabey in the *Cruseturner* opinion is particularly relevant.

> Thus, when the trustee abandons property, the property stands as if no bankruptcy had been filed and the debtor enjoys the same claim to it and interest in it as he held previous to the filing of bankruptcy . . . Although case law characterization of the revesting of property in the debtor has been

> referred to as "legal fiction" . . . application in this context is appropriate in light of both the legislative history and the plain meaning of the applicable statutory provisions.

In re Cruseturner, 8 B.R. at 591-592.

By operation of the "legal fiction" as to title of abandonment property, the Quanta Trustee would stand as if he never had any interest in the polluted inventories. He would therefore be immune from prosecution for violation of environmental laws, subject to liability only if he undertook some prohibited act such as pouring the waste oil down a sanitary sewer.

Sound policy considerations support continuation of the "legal fiction" surrounding abandonment in a bankruptcy liquidation proceeding in today's world. Midlantic asks, who would choose to serve as a trustee in bankruptcy if personal liability would attach to such a trustee for environmental problems arising because of prepetition conduct of the debtor? Indeed, in its opinion concerning the Long Island City abandonment, the Court of Appeals indicated that by abandoning the contaminated waste oil the Trustee may be guilty of a felony under New York law. *City of New York* v. *Quanta Resources Corp.,* 739 F.2d at 921. Clearly, no person would accept such a perilous responsibility and the bankruptcy system would grind to a halt in any case where potential environmental issues could arise.

This exact problem surface in *In re Charles George Land Reclamation Trust,* 30 B.R. 918 (Bkrtcy. Ma. 1983). In that case, no person was willing to accept the risk of personal liability arising under state and federal environmental laws by serving as a Chapter 7 trustee for an estate with grave environmental problems. *Id.* at 924. As

a result, the Bankruptcy Court dismissed the Chapter 7 proceeding citing as reasons the lack of resources, expertise and a qualified trustee. *Id.* This abdication of responsibility is the end product of an irrational interpretation of 11 U.S.C. §554(a). This Court should address this very important issue with a clear and direct statement limiting liability of a trustee under the doctrine of *Brown* v. *O'Keefe,* 300 U.S. 598, 602, 57 S.Ct. 543, 81 L.Ed. 827 (1937).

B. The Court of Appeals erred in concluding that Congress intended that abandonment be conditioned upon compliance with state environmental protection laws.

The starting point in statutory interpretation is the language of the statute—in this case 11 U.S.C. §554(a). *Reiter* v. *Sonotone Corp.,* 442 U.S. 330, 337, 99 SCt. 2326, 2330, 60 L.Ed.2d 931 (1978). If the statutory language is clear, it is ordinarily conclusive. *United States* v. *Clark,* 454 U.S. 555, 561, 102 S.Ct. 895, 809, 70 L.Ed.2d 768 (1982). It is not a function of the United States Supreme Court or any other court to sit as a super-legislature and create statutory distinctions where none was intended. *American Tobacco Co.* v. *Patterson,* 456 U.S. 63, 72, 102 S.Ct. 1534, 1539, 71 L.Ed.2d 748 (1982) (footnote 6), *citing, Griswald* v. *Connecticut,* 381 U.S. 479, 482, 85 S.Ct. 1678, 1680, 14 L.Ed.2d 510 (1965). Absent a clearly expressed legislative intention to the contrary, the statutory language must be regarded as conclusive by a reviewing court. *Consumer Product Safety Comm'n* v. *GTE Sylvania, Inc.,* 447 U.S. 102, 108, 100 S.Ct. 2051, 2055, 64 L.Ed.2d 766 (1980).

In construing 11 U.S.C. §554(a), the Court of Appeals found clear language which on its face did not condition abandonment upon compliance with state environmental

legislation. It then noted that there is no specific legislative history of §554(a). *City of New York* v. *Quanta Resources Corp.*, 739 F.2d at 916. Nonetheless, the Court of Appeals searched long and hard to find what it determined to be a legislative intent to condition abandonment upon compliance with local environmental laws. Midlantic respectfully asserts that the Court of Appeals erred by looking beyond the express language of §554(a) to create a statutory distinction that was not intended by Congress.

The Third Circuit first examined several cases decided prior to enactment of the statutory abandonment provision which held that a trustee's ability to abandon burdensome property is subject to police power regulations. The first case was *Ottenheimer* v. *Whitaker*, 198 F.2d 289 (4th Cir. 1952), *aff'g*, 102 F.Supp. 193 (D.Md. 1952). In *Ottenheimer*, the Court of Appeals held that trustee could not abandon a number of dilapidated barges in Baltimore harbor when abandonment would violate a federal statute prohibiting the sinking of vessels in a navigable channel. *Id.* at 290. The absence of a statutory provision governing abandonment weighed heavily in the balancing analysis undertaken by the Fourth Circuit.

> It seems obvious to us that a rule which is not provided by statute but built up by the courts to facilitate the administration and distribution of the assets of a bankrupt estate should not be extended so as to reach such an unreasonable and unjust result. The judge-made rule must give way when it comes in conflict with a statute enacted to ensure the safety of navigation . . .

Id. at 290. As a result, it stands clear that the analysis of the *Ottenheimer* Court would have markedly differed if 11 U.S.C. §554(a) had been in effect at the time of that trustee's application for abandonment.

The second case relied upon by the Third Circuit in *Quanta* was *In re Lewis Jones, Inc.*, 1 Bkr.Ct. Dec. 277 (Bkrtcy. E.D.Pa. 1974). In that case, a trustee of a public utility was barred from abandoning underground steampipes and vents when abandonment would expose the public to risk of accident and injury. The *Lewis Jones* Court heavily relied upon the *Ottenheimer* case in reaching this decision and, in fact, did not cite to any other case in support of the principle that the power to abandon is subject to police power regulations. Therefore, it must also be conceded that the analysis of the *Lewis Jones* Court would also dramatically change if §554 had been enacted prior to the time of that decision.

Moreover, *Lewis Jones* is also distinguishable because of the particular equitable considerations present in that case. In *Lewis Jones*, it was estimated that the trustee could adequately protect the public safety by sealing the underground pipes at a cost of approximately $64,000. *In re Lewis Jones*, 1 Bkr. Ct. Dec. at 278-279. Insofar as the bankruptcy estate contained over $325,000, the *Lewis Jones* Court determined that an expenditure of $64,000 would not be unreasonable. *Id.* at 280. In contrast, the Quanta estate does not contain sufficient funds for cleanup of either the Edgewater or Long Island City facilities. There would be no "cushion" for creditors if the Trustee had to clean up the property prior to abandonment. As a result, the Court of Appeals erred in relying upon the particular equitable considerations so important to the decision of the *Lewis Jones* Court.

The Third Circuit also looked to *In re Chicago Rapid Transit Co.*, 129 F.2d 1 (7th Cir. 1942), *cert. denied*, 317 U.S. 683, 63 S.Ct. 205, 87 L.Ed. 547 (1942), for guidance on the legislative intent issue. There, the Seventh Circuit determined that trustees for a railroad in reorganization could not abandon services on a branch line absent

approval of local regulatory authorities. *Id.* at 5. Two factors distinguish *Chicago Rapid Transit* from the case at bar. First, the debtor was in reorganization rather than in liquidation. Second, the abandonment directly related to operation and management of the debtor's business as opposed to the situation in Quanta where the Trustee was attempting to fulfill his statutory directive to wrap up the estate.[10]

As noted by Judge Gibbons in his dissenting opinion below, not one of the above-referred decisions is persuasive under the Bankruptcy Reform Act of 1978. Focusing upon *Ottenheimer* and *Lewis Jones,* Judge Gibbons commented that:

> Neither of these opinions, however, is persuasive under the 1978 Bankruptcy Reform Act. Both substitute slogans about equity for an analysis of the purpose of bankruptcy proceedings. Both, moreover, were decided prior to the enactment of the Bankruptcy Reform Act of 1978, and its codification in 11 U.S.C. §554 (1982) of the express authority for trustees to decline to undertake responsibility for property which cannot benefit the estate. Thus there was no statutory provision permitting trustees to abandon burdensome property at the time of those decisions. Such an express statutory provision now exists. Moreover, Congress did *not* see fit to provide an exception to this statutory power, whether for the public interest or any other purpose, as it has in other areas. *Compare* 11 U.S.C. §362(a) (1982) (exception to automatic stay); *Penn Terra Ltd.* v. *Department of Environmental Resources,* 733 F.2d 267, 274-79 (3d Cir. 1984) (injunction to enforce compliance with state laws is not a money judgment, and is therefore not subject to §362 stay) with 11 U.S.C. §554 (1982). Thus *Ottenheimer* and *Lewis Jones* are not helpful.

[10] The requirement that a trustee manage and operate property in a reorganization proceeding in accordance with the state law has since been codified at 28 U.S.C. §959(b).

City of New York v. *Quanta Resources Corp.,* 739 F.2d at 923-924. Thus, the *Quanta* majority's reliance upon these older cases stands misplaced in view of the changes to the bankruptcy laws that were enacted in 1978.

The comparison drawn by Judge Gibbson in his dissent between §554(a) and other statutory provisions further demonstrates that Congress did not intend for abandonment to be conditioned upon environmental compliance. The regulatory exception to the automatic stay provision of 11 U.S.C. §362 was noted by this Court in *Ohio* v. *Kovacs,* —— U.S. ——, 105 S.Ct. 705, 711, 83 L.Ed. 2d 649 (1985). In §362 of the Bankruptcy Code, Congress created a specific exception to the general rule that commencement or continuation of actions against a debtor in bankruptcy are automatically stayed. If Congress intended that a similar exception apply to abandonment under §554(a), specific language would have also been incorporated.

That conclusion is buttressed by reference to 28 U.S.C. §959(b) which requires a trustee or receiver appointed by any United States Court to manage and operate property in his possession in accordance with state law. Yet, as noted in a prominent treatise, this duty does not extend to a trustee who is liquidating estate assets as opposed to carrying on the business of a debtor.

> But Section 959(b) applies only to the Receiver in his operation of property in his possession. It does not apply to the distribution of the estate,

> and does not require the federal receivership court to comply with state laws regulating the distribution of funds in the receivership . . .

7-Pt. 2 J. Moore and J. Lucas, *Moore's Federal Practice* §66.04(4) at 1913 (2d Ed. 1982); *see also, Austrian* v. *Williams,* 216 F.2d 278, 285 (2d Cir. 1954), *cert. denied,* 348 U.S. 953, 75 S.Ct. 441, 99 L.Ed. 745 (1954) (holding that the mere collection and liquidation of assets did not constitute the carrying on of a debtor's business).

Additional support is found in the decision of the Eighth Circuit Court of Appeals in *State of Mo.* v. *U.S. Bkrtcy. Court, Etc.,* 647 F.2d 768 (8th Cir. 1981), *cert. denied,* 454 U.S. 1162, 102 S.Ct. 1035, 71 L.Ed. 2d 318 (1982). In that case, the State of Missouri contended that a Chapter 11 trustee planned to operate a grain warehouse without a state license in violation of 28 U.S.C. §959(b). Writing for the Circuit Court, Judge Bright recognized that, in operations, the trustee must act consistent with the dictates of §959(b). *Id* at 778. However, Judge Bright went on to note that:

> We add that any authorized action by the trustee to liquidate or sell the grain appears to fall within the power of the bankruptcy court to liquidate the debtors' assets under the Bankruptcy Act. We doubt, therefore, that a trustee must obtain a state license solely for liquidation.

Id., note 18. Similarly, NJDEP cannot here demand that the Quanta Trustee bring the Edgewater facility into full environmental compliance when the Trustee's role is limited to the liquidation of estate assets.

Based upon a review of every authority relied upon by the Court of Appeals, one must conclude that Congress

did not intend that the Trustee's power to abandon worthless property under §554(a) be limited by environmental regulations. As noted by this Court in footnote 12 of the *Kovacs* opinion:

> Had no receiver been appointed prior to Kovacs' bankruptcy, the trustee would have been charged with the duty of collecting Kovacs' nonexempt property and administering it. If the site at issue were Kovacs' property, the trustee would shortly determine whether it was of value to the estate. If the property was worth more than the costs of bringing it into compliance with state law, the trustee would undoubtedly sell it for its net value, and the buyer would clean up the property, in which event whatever obligation Kovacs might have had to clean up the property would have been satisfied. If the property were worth less than the cost of cleanup, the trustee would likely abandon it to its prior owner, who would have to comply with the state environmental law to the extent of his or its ability.

Ohio v. *Kovacs,* 105 S.Ct. at 711.

By focusing upon the important policy of protecting the public health by regulating the disposal of toxic wastes, the Court of Appeals forged an exception to the abandonment statute that is not supported at law. The decisions represent an impermissible intrusion into the legislative arena and should be reversed.

Moreover, existing law contains adequate measures to protect the public safety.[11] Under N.J.S.A. 58:10-23.11f(f)

[11] In addition, in this case, abandonment would in all likelihood vest title to the oil in Quanta's landlords, Frola and Von Dohlin, who would remediate the contamination so as to render their land once again valuable.

(West Supp. 1983), NJDEP could have cleaned up the Edgewater site and claimed a "first priority claim and lien paramount to all other claims and liens" on the Quanta property. Since NJDEP failed to take any action to clean up the Edgewater property and thus trigger a priority claim to Quanta assets, this Court should not endorse the decision of the Third Circuit to condition abandonment of the contaminated oil upon compliance at the expense of secured creditors such as Midlantic.

POINT III

Conditioning abandonment of burdensome property upon environmental compliance frustrates full effectuation of the objectives of federal bankruptcy legislation and therefore violates the supremacy clause.

The Court of Appeals' construction of 11 U.S.C. §554(a) also raises a serious question of Constitutional law arising under the supremacy clause, U.S. Const. Art. VI, cl. 2. Specifically, that question is whether state environmental laws upon which abandonment of burdensome assets in a liquidation proceeding would be conditioned are invalid insofar as they "stand as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress." *See, Michigan Canners & Freezers Assn.* v. *Agricultural Marketing and Bargaining Board,* —— U.S. ——, 104 S.Ct. 2518, 2523, 81 L.Ed.2d 399, 406 (1984); *Hines* v. *Davidowitz,* 312 U.S. 52, 67, 61 S.Ct. 399, 85 L.Ed. 581 (1941). As in *Perez* v. *Campbell,* 402 U.S. 637, 91 S.Ct. 1704, 29 L.Ed.2d 233 (1971), the supremacy clause analysis focuses upon the objectives of federal bankruptcy legislation.

In page after page of involved analysis, the Court of Appeals in Quanta wrestled with the supremacy clause

issue. *City of New York* v. *Quanta Resources Corp.,* 739 F.2d 915-922. Applying the two-step test set forth in *Perez* v. *Campbell,* 402 U.S. at 644, 91 S.Ct. at 1708-1711, 29 L.Ed. 2d at 239, the Third Circuit first examined the purposes of the laws at issue and then determined whether the state environmental laws frustrated the objectives of the Bankruptcy Code. *City of New York* v. *Quanta Resources Corp.,* 739 F.2d at 915. Midlantic respectfully asserts that the Court of Appeals erred in concluding that the state laws do not frustrate the principal duty of a trustee under 11 U.S.C. §704 to collect and reduce to money the property of the estate and to close the estate in an expeditious manner.[12]

Midlantic would offer one specific example to properly focus the attention of the Court on the supremacy issue. In 1983, the New Jersey Legislature enacted the Environmental Cleanup Responsibility Act ("ECRA"), N.J.S.A. 13:1K-6 *et seq.* (West Supp. 1984). Through ECRA, an owner or operator of certain industrial establishments is required to notify NJDEP in advance of a decision to stop, sell or transfer operations. N.J.S.A. 13:1K-9(a)(1) and (b(1) (West Supp. 1984). ECRA also requires preparation of cleanup plans to correct environmental problems along with submission of surety bonds to guarantee cleanup. N.J.S.A. 13:1K-9(a)(2) and (b)(3) (West Supp. 1984). Failure to comply with any provision of ECRA triggers (1) voiding of the transfer, (2) strict liability for cleanup costs and (3) substantial civil penalties. N.J.S.A. 13:1K-13 (West Supp. 1984).

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[12] *See,* S. Rep. No. 95-989, 95th Cong., 2d Sess. 93 (1978), *reprinted in* (1978) U.S. Code Cong. & Ad. News 5787, 5879 and H.R. Rep. No. 95-595, 95th Cong., 1st Sess. 379 (1977), reprinted in, (1978) U.S. Code Cong. & Ad. News 5963, 6335.

Under the decisions below, the Quanta Trustee must not abandon the Edgewater, New Jersey property but must instead bring the site into environmental compliance. Although N.J.S.A. 13:1K-8(b) (West Supp. 1984) excepts the *initiation* of bankruptcy proceedings from ECRA responsibilities, it will undoubtedly be argued that subsequent action by the Trustee must conform to ECRA standards. Thus, the Trustee must post bonds, draft cleanup plans and look not to the Bankrutpcy Court but instead to NJDEP for ratification of decisions central to estate administration. NJDEP would thereby usurp the power of the Bankruptcy Court in violation of the supremacy clause.

Morever, Section 8 of ECRA, N.J.S.A. 13:1K-12 (West Supp. 1984), provides that "(n)o obligations imposed by this act shall constitute a lien or claim which may be limited or discharged in a bankruptcy proceeding." Thus, under the decision below, NJDEP would assert that notwithstanding the specific discharge provision of federal bankruptcy law, 11 U.S.C. §727, the Trustee and the *Quanta* estate would remain obligated for ECRA cleanup responsibility as a condition to any transfer of estate assets. This requirement directly conflicts with the discharge provisions of federal bankruptcy law and is invalid under the supremacy clause.

State environmental laws such as ECRA serve the laudible purpose of protecting the public health through regulation of toxic waste disposal. However, such laws may not frustrate the operation of federal law simply because the state legislature in passing the laws had some purpose in mind other than one of frustration. *Pacific Gas and Electric Company* v. *State Energy Resources Conservation & Development Commission*, 461 U.S. 190, 216, 103 S.Ct. 1713, 75 L.Ed.2d 752, 773 (1983) (footnote 28); *Perez* v. *Campbell*, 402 U.S. at 651, 29 L.Ed.2d at

244-245. The supremacy clause commands that conflicting state laws must fall when they stand as an obstacle to the objectives of federal law.

CONCLUSION

Midlantic National Bank has demonstrated that the decisions of the Third Circuit Court of Appeals below conflict with the rule of statutory construction outlined in *United States* v. *Security National Bank*, 459 U.S. 70, 103 S.Ct. 407, 74 L.Ed.2d 235 (1982). Midlantic has further demonstrated that the Court of Appeals erred in concluding that Congress intended that abandonment under 11 U.S.C. §554(a) be conditioned upon compliance with state environmental laws. Finally, Midlantic has shown that the Court of Appeals erred in concluding that the claims of the state regulatory agencies in these actions are not barred by the supremacy clause of the United States Constitution.

Wherefore, Midlantic National Bank respectfully requests that the decisions of the Court of Appeals be reversed with instruction to affirm the lower court orders approving the abandonment of the burdensome assets of the estate.

Respectfully submitted,

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April 4, 1985

No. 84-805 (5)
No. 84-801 (4)

In The

Supreme Court of the United States

October Term, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE CITY OF NEW YORK AND STATE OF NEW YORK, and THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondents.

MIDLANTIC NATIONAL BANK,
Petitioner,

v.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR PETITIONER THOMAS J. O'NEILL, TRUSTEE

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QUESTIONS PRESENTED

1. Whether the right of a trustee in Bankruptcy pursuant to Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), to abandon property of the estate, which admittedly is burdensome to the estate and of inconsequential value to the estate, can be restricted by a state as a result of pre-petition conduct of the debtor.

2. Whether the Court of Appeals' reliance upon an exception to the automatic stay contained in Section 362 of the Bankruptcy Code, 11 U.S.C. Section 362, as a basis for judicially inserting an exception to the right of abandonment into Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), is inconsistent with this Court's decisions in *Ohio v. Kovacs,* 105 S. Ct. 705 (1985) and *NLRB v. Bildisco and Bildisco,* 104 S. Ct. 1188 (1984).

3. Whether the decisions of the Court of Appeals are inconsistent with this Court's decision in *United States v. Security Industrial Bank,* 459 U.S. 70 (1982), in construing the Bankrutpcy Code as requiring a trustee in bankruptcy to expend assets of the estate to effect an environmental cleanup of facilities operated by the debtor prior to the filing of the bankruptcy petition, which are of no value to the estate, thereby raising constitutional questions arising out of the "takings clause" of the Fifth Amendment.

4. Whether denying a trustee in bankruptcy the right to abandon property of the estate pursuant to Section 554(a) of the Bankruptcy Code because of purported prepetition violations of state environmental laws is violative of the Supremacy Clause of the federal constitution.

5. Whether judicial imposition of conditions upon the right of a trustee in bankruptcy to abandon property of the estate pursuant to Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), will impair bankruptcy policy and frustrate effectuation of the objectives of the federal Bankruptcy Code.

6. Whether "abandonment of property of the estate" by a trustee in bankruptcy pursuant to Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), can constitute a violation of state environmental laws and regulations.

7. Whether 28 U.S.C. Section 959(b) is applicable to a bankruptcy trustee in a liquidation proceeding and can serve as a basis for denying a trustee the right to abandon property under 11 U.S.C. Section 554(a).

8. Whether a state's claim for reimbursement of expenses for the environmental cleanup of property of the debtor is entitled to priority or administrative expense status under the Bankruptcy Code.

PARTIES

Appellants in Third Circuit Case No. 83-5142 ("New York Case") were the City of New York and the State of New York. Also appearing in that case, as *amici curiae*, were the State of Pennsylvania, the Department of Environmental Resources for the State of Pennsylvania and the State of New Jersey. Appellant in Third Circuit Case No. 83-5730 ("New Jersey Case") was the New Jersey Department of Environmental Protection. Thomas J. O'Neill, Trustee in Bankruptcy of Quanta Resources Corporation,[1] debtor, was an appellee in both cases. Midlantic National Bank and James V. Frola and Albert Von Dohlin were appellees in the New Jersey Case.

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[1]Quanta Resources Corporation, a Delaware Corporation, is a wholly owned subsidiary of Quanta Holding Corporation, a subsidiary of Waste Recovery, Inc., which in turn was a subsidiary of Warburg Paribas Becker, Inc.

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In The
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ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR PETITIONER THOMAS J. O'NEILL, TRUSTEE

OPINIONS BELOW

The opinions of the Court of Appeals for Case No. 83-5142 (New York) and Case No. 83-5730 (New Jersey) are reported at 739 F.2d 913 and 739 F.2d 927 respectively. The Memorandum Opinion of the District Court in *State of New York and the City of New York v. Thomas J.*

O'Neill, Trustee in Bankruptcy of Quanta Resources Corp. (App. G, 52a to 60a)[2] and the opinion of the Bankruptcy Court in the case *State of New York and City of New York v. Thomas J. O'Neill* (App. K, 69a to 75a) are unreported.

JURISDICTION

The judgment of the Court of Appeals in Case No. 83-5142 (App. D, 45a) was entered on July 20, 1984. The Amended Judgment in Case No. 83-5730 (App. E, 47a) was entered on July 25, 1984. On August 16, 1984 the Court of Appeals denied rehearing. (App. F, 49a). Petitions for writs of certiorari were filed on November 14, 1984, and granted on February 19, 1985, at which time the cases were consolidated with the Petition filed on behalf of Midlantic National Bank. The jurisdiction of this Court is invoked under 28 U.S.C. Section 1254(1).

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

The constitutional provisions involved are the Supremacy Clause of Article VI and the "takings clause" of the Fifth Amendment. The provisions of the Bankruptcy Code involved are Sections 362, 554, and 704, 11 U.S.C.

[2]References to the Appendix are to the Appendix to the Petition for Certiorari filed by Thomas J. O'Neill, Trustee of Quanta Resources Corp.

Sections 362, 554, and 704. The case also involves interpretation of 28 U.S.C. Section 959(b). These provisions are printed in the Appendix to the Petition for Certiorari. (App. L, 76a-79a).

STATEMENT OF THE CASE

The two cases before the Court, although involving two separate sites, one in New York and the other in New Jersey, arise out of the same bankruptcy proceeding. They present the question of the proper construction of Section 554(a) of the Bankruptcy Code entitled *Abandonment of Property of the Estate,* 11 U.S.C. Section 554(a), and the inter-relationship of this section with other state and federal laws.

The question is presented in the context of the bankruptcy liquidation of a corporation which had engaged in the business of treatment of waste oils, and the attempt by the Trustee in Bankruptcy to abandon real and personal property of the estate which is alleged to have been contaminated through pre-petition conduct of the debtor. The Trustee's abandonment is opposed by the respective environmental agencies of New York and New Jersey, who seek to compel the Trustee to clean up the sites.

On October 6, 1981, Quanta Resources Corp. ("Quanta") filed a voluntary petition under Chapter 11 of the Bankruptcy Code, 11 U.S.C. Section 1101, *et seq.* On November 12, 1981, on motion of the debtor, the proceedings were converted to liquidation under Chapter 7, 11 U.S.C.

Section 701, *et seq.* Petitioner, Thomas J. O'Neill, was appointed Trustee on November 18, 1981.

The debtor corporation had operated facilities in Edgewater, New Jersey and Long Island City, New York. The New York property was owned by the debtor, while the New Jersey site was leased from two individuals, James Frola and Albert VonDohlin, appellees before the Third Circuit in the New Jersey case. All operations of the debtor corporation had ceased prior to the bankruptcy proceedings.

New York

Upon his appointment, the Trustee obtained an appraisal report of the property located at 37-80 Review Avenue, Long Island City, New York, which contained the following description:

> The subject property has been used for many years as a storage facility for waste oil and is improved with a wide variety of fuel storage tanks. We have been advised that many of these tanks now hold waste oil which is contaminated and effectively, the tanks have little or no market value. Also located on the site are several small concrete block buildings that were used in connection with this operation. In the judgment of the appraiser, the age and condition of these buildings are such that they have no value and should be removed.

The appraiser estimated the fair market value of the property as $535,000.00, but stated for "forced sale" purposes he would discount this value by 20% to $428,000.00. Mortgages on the property exceeded the "forced sale" value.

A considerable quantity of waste oil, sludge and other hazardous wastes, including oil contaminated with PCB's, was stored on the property at the time of the filing of the bankruptcy petition. It was estimated that the cost to dispose of the contaminated waste oil properly and otherwise clean up the site would be in excess of one million dollars.[3] Neither the "fair market" or "forced sale" estimates took into consideration the contaminated state of the property nor the expenditures which would be necessary in order to dispose of the oil on the site and render the property marketable.

The property was unquestionably valueless to the Trustee. Additionally, at the outset of the case, the Trustee was required to maintain 24 hour guard service at a cost in excess of $1,100.00 per week, a substantial burden to the estate.

At the initial hearing before the Bankruptcy Court on the application to abandon, the Trustee testified that he personally had borrowed $20,000.00, much of which had gone to continue the security. The Trustee simply had no funds whatsoever to pay for continued security, much less to undertake a cleanup.

On March 18, 1982, upon request of the Trustee, the Clerk of the Bankruptcy Court issued a notice to creditors of "sale by public auction or abandonment" scheduled for April 5, 1982. The notice advised that if the Trustee did not receive an offer in excess of liens on the property, he would abandon the property. No offers were received.

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[3]According to New York's Brief before the Third Circuit, following the Trustee's abandonment, the City and State undertook a cleanup operation and expended 2.5 million dollars.

Greenpoint Oil Corp. ("Greenpoint") subsequently offered to purchase the property, subject to mortgages and certain other liens, for a total price of $3,000.00. This offer was approved by the Bankruptcy Court. Counsel for Greenpoint later advised the Trustee, however, that Greenpoint did not intend to proceed with the purchase because of hazardous conditions and violations existing at the property of which Greenpoint was not aware at the time of the offer. On June 22, 1982, on application of Greenpoint, the Bankruptcy Court voided the approval of the offer.

Although the Trustee believed that the property should then be deemed to have been abandoned as of April 5, 1982, a new notice of proposed abandonment was mailed to all creditors on May 25, 1982. In response to the second notice to creditors, the State of New York filed an objection with the Bankruptcy Court on June 4, 1982. On June 7, 1982, the City of New York also filed an objection.

Oral argument on the objections was conducted before Bankruptcy Judge D. Joseph DeVito on June 8, 1982, at which time the Court directed the filing of additional briefs. On or about June 15, 1982, the State of New York filed a Memorandum in Opposition to Abandonment in which, for the first time, the State requested that the Court order that any money spent by the State or City to dispose of the waste be deemed a first lien on the property with priority over any other mortgages and liens.[4] No notice of the application to impose a lien was given to the other lienholders on the property.

[4]As of that date, no money had been expended by the City or State.

Following additional argument on June 22, 1982, the Bankruptcy Court authorized the Trustee to abandon the property. In refusing to direct the Trustee to undertake a cleanup of the site, Judge DeVito stated:

> The City and State are in a better position in every respect than either the trustee or debtor's creditors to do what needs to be done to protect the public against the dangers posed by the PCB contaminated facility . . . For this Court to grant the relief requested by the Attorney General would do little else than to put into play an exercise in futility, and would possibly delay the parties who could be chargeable with the cleanup of the property or who have other interests to permit them to move in. That should go forth as quickly as possible and I think this determination will work in that direction.

(App. K, 73a to 74a). The claim to entitlement to a lien was rejected by the Court as unauthorized under the Bankruptcy Code. An Order incorporating the terms of the Court's oral decision was entered on July 7, 1982, effective June 22, 1982, *nunc pro tunc*. (App. J, 66a to 68a).

Notices of Appeal to the District Court were filed on July 16, 1982. Oral argument was conducted before District Court Judge Frederick B. Lacey, on January 24, 1983. At that time, and in a Memorandum Opinion (App. G, 52a to 60a), Judge Lacey affirmed the decision of the Bankruptcy Court. The New York appeal was docketed in the Third Circuit on February 28, 1983.

As noted above, cleanup of the property has been undertaken by New York, and what is now sought from the Trustee is solely payment of New York's claim for reimbursement of the money expended. The issue of the Trustee's obligation to clean up the site therefore has been mooted.

New Jersey

Quanta also operated a waste oil treatment facility located at 1 River Road, Edgewater, New Jersey, consisting of storage and product tanks and equipment for the processing of oil. In June, 1981, a sampling of the waste oil at the site by the New Jersey Department of Environmental Protection ("NJDEP") determined that levels of PCB's were present in the oil in excess of permissible levels. On July 2, 1981, Quanta agreed to cease its operations upon NJDEP's request. NJDEP further directed that certain remedial steps be undertaken by Quanta. The filing of the bankruptcy petition intervened.

For the Trustee to implement the remedial measures would have exhausted all the assets in the estate without any resulting benefit to the estate. The Trustee had no alternative but to seek authorization to abandon.

The New Jersey site was leased by the debtor and therefore the application for abandonment was limited to personal property consisting mainly of the oil in the tanks. An Order was entered by the Bankruptcy Court on May 20, 1983, authorizing the abandonment of the property effective May 17, 1983, *nunc pro tunc* (App. I, 64a to 65a).

Since the identical issue presented in the New Jersey case was already pending before the Court of Appeals, a notice of appeal by agreement to the Court of Appeals under 28 U.S.C. Section 1293(b) was filed on behalf of the NJDEP on September 21, 1983.

The New York case was argued before the Court of Appeals for the Third Circuit on October 24, 1983. No argument was heard in the New Jersey case. A divided Court of Appeals announced its decision in both matters on July 20, 1984, reversing the decisions of the Bankruptcy and District Courts. *In the Matter of Quanta Resources Corp., etc.*, 739 F.2d 913 (3rd Circuit 1984); *In re Quanta Resources Corp., debtor, etc.*, 739 F.2d 927 (3rd Circuit 1984). The Trustee filed a Petition for Rehearing in both matters, but on August 16, 1984, rehearing was denied (App. F, 49a to 51a).

Perhaps the most concise critique of the majority opinion is to be found in Judge Gibbons' dissent in the New York case in which he took exception with the majority decision on the following counts:

1) By forcing the trustee to take possession of property in which there is no equity, the court serves no interest that the bankruptcy laws address. (739 F.2d 923).

2) There is no legislative history suggesting that the court may alter or amend the language of 11 U.S.C. Section 554(a). (739 F.2d 923).

3) Under federal law, the trustee may abandon the property. (739 F.2d 923).

4) Congress did not see fit to provide an exception to the statutory power of abandonment under 11 U.S.C. Section 554(a), whether for the public interest or any other purpose, as it has in other areas. (739 F.2d 924).

5) The majority opinion is inconsistent with the Supreme Court's recent decision in *United States v. Security Industrial Bank,* 459 U.S. 70 (1982). (737 F. 2d 924).

6) The majority's construction of the Act raises a substantial question under the taking clause of the Fifth Amendment. (739 F. 2d 925).

7) The plain language of 11 U.S.C. Section 554(a) permits abandonment in this case; moreover, there is no

legislative history to that section providing any exceptions to the statute or expressing any intent contrary to abandonment by a trustee of property found to be burdensome or of inconsequential value. (739 F. 2d 925).

8) The majority opinion sidesteps the key issue of the priority, if any, of the states' claims. (739 F. 2d 925).

9) The majority's reliance on 28 U.S.C. Section 959 (b) is off the mark. (739 F. 2d 926).

10) The suggestion that the cleanup cost might be classified as a "preservation expense" of a property is preposterous. (739 F. 2d 926).

Judge Gibbons also raised the question left unanswered by the majority of how the trustee can reach into creditors' pockets for the cost of the cleanup, and if he can, which creditor's pocket. (739 F. 2d 923). He then concluded his dissenting opinion with the observation that:

> We surely will have to affirm later when the district court points to the obvious fact that there must be a source of funds before expenditures can be made. (739 F. 2d 927).

At this point, the administration of the debtor's estate is virtually complete. All assets, other than those abandoned by the Trustee, have been liquidated. Distribution was made to secured creditors at the time the assets securing their liens were sold, and administrative expenses incurred by the trustee, including but not limited to salaries and use and occupancy claims, have been paid to the extent funds were available. The Trustee has no money from which to finance any cleanup of either facility or to reimburse the states for their cleanup costs.

SUMMARY OF ARGUMENT

Under Section 554(a) of the Bankruptcy Code, 11 U.S.C. Section 554(a), after notice and a hearing, a trustee in bankruptcy may abandon any property of the estate that is burdensome to the estate or that is of inconsequental value to the estate. The two sites involved in this case, one in New York and one in New Jersey, which contained oil contaminated with PCB's, were of no value and were burdensome to the estate. The trustee did not have sufficient assets available to finance cleanup of the sites, the cost of which would have far exceeded the value of the two properties in an uncontaminated condition. Any cleanup therefore would not have benefitted the estate.

The trustee had no alternative but to seek leave of the Bankruptcy Court to abandon the property. Abandonment was both appropriate and authorized under the Bankruptcy Code.

The decision of the Court of Appeals runs contrary to the decisions of this Court in *Ohio v. Kovacs,* 105 S. Ct. 705 (1985), and *NLRB v. Bildisco and Bildisco,* 104 S. Ct. 1188 (1984), in inserting into the Bankruptcy Code an exception to the right of abandonment under Section 554 (a), where no such exception was included or intended by Congress.

The duty of a trustee in liquidation proceedings is to reduce the debtor's property to money as expeditiously as possible so as to secure funds for distribution to general creditors in accordance with the scheme of distribution of the Bankruptcy Code. To require a trustee to retain and administer property that is valueless is contrary to

this fundamental objective of bankruptcy. For the trustee to expend other assets of the estate to clean up the sites and thereby satisfy the claims of the governmental bodies would in effect create preferences not recognized by the Bankruptcy Code.

If, as the majority held, the right of abandonment can be restricted by state and local law, the full effectuation of the objectives of federal bankruptcy legislation will be frustrated, thereby contravening the Supremacy Clause, U.S. Const. Art. VI Cl. 2.

To require a trustee in bankruptcy, who does not have sufficient assets, to administer valueless property and exhaust all other assets of the estate, which otherwise would be available for distribution to creditors, both secured and unsecured, would be violative of the Fifth Amendment to the Constitution. Such a construction of the Bankruptcy Code would further be inconsistent with this Court's decision in *United States v. Security Industrial Bank,* 459 U.S. 70 (1982).

To deny the trustee the right to abandon worthless and burdensome property would impair bankruptcy policy without any corresponding advancement of environmental policy.

A trustee in bankruptcy cannot be found to have violated state environmental laws based upon pre-petition conduct of the debtor. 29 U.S.C. 959(b) does not constitute a ban upon abandonment by the trustee under the circumstances of this case, the Trustee not having operated the debtor's business and not having violated any state laws.

The Court of Appeals failed to clearly focus on the critical and fundamental distinction in bankruptcy law between pre-bankruptcy and post-bankruptcy rights against the debtor.

ARGUMENT

Under The Facts Of This Case, The Trustee In Bankruptcy Was Entitled To Abandon The Property Pursuant To 11 U.S.C. Section 554(a).

A. The construction of Section 554(a) advanced by the majority is contrary to this Court's rule of construction announced in Ohio v. Kovacs, 105 S. Ct. 705 (1985), and NLRB v. Bildisco and Bildisco, 104 S. Ct. 1188 (1984), in judicially inserting an exception into the Bankruptcy Code where no such exception was intended or included by Congress.

Any analysis of the issues in this case must begin with the unchallenged factual finding of the Bankruptcy Court that the property was burdensome and of inconsequential or no value to the estate. The next step is to examine the statute in question, Section 554(a) of the Bankruptcy Code, which provides that:

> After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

11 U.S.C. Section 554(a). The purposes of this section as noted by the majority are to enable the trustee to rid the estate of burdensome or worthless assets thereby

speeding the administration of the estate and protecting the estate from diminution. Abandonment serves the creditors' interest in expeditiously obtaining a fair amount in settlement of their claims. *In the Matter of Quanta Resources Corp., etc.*, supra at 915.

In imposing conditions upon the trustee's right to abandon, the Court of Appeals relied upon the exception to the automatic stay provisions of Section 362 of the Bankruptcy Code, 11 U.S.C. Section 362, which provides that "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power" is not stayed by the filing of a bankruptcy petition. 11 U.S.C. Section 362(b)(4).

In *Ohio v. Kovacs,* 105 S. Ct. 705 (1985), the Supreme Court took the opportunity to disapprove of attempts to impose conditions or limitations upon various provisions of the Bankruptcy Code where the plain reading of the section did not allow such conditions or limitations. In *Kovacs,* Ohio proposed a strained interpretation of the definition of "claim" under Section 101 to support its position that an obligation under an affirmative injunction was not a claim and therefore not dischargeable in bankruptcy.

In rejecting this argument, the Court cited areas where Congress had expressly created exemptions:

> Congress created exemptions from discharge for claims involving penalties and forfeitures owed to a governmental unit, 11 U.S.C. Section 523(a)(7), and for claims involving embezzlement and larceny, Section 523(a)(4). If a bankruptcy debtor has committed larceny or embezzlement, giving rise to a remedy of either damages or equitable restitution under state law, the resulting liability for breach of an obligation created by law is clearly a claim which is nondischargeable in bankruptcy.

105 S. Ct. at 709, Footnote 5. The Court held that such examples of limitations expressly included in the Code by Congress refuted rather than supported Ohio's attempt to carve out a new exception.

This Court had previously addressed a similar issue in *NLRB v. Bildisco and Bildisco,* 104 S. Ct. 1188 (1984), where it was argued that collective bargaining agreements were not included within the general scope of Section 365(a) of the Bankruptcy Code, 11 U.S.C. Section 365(a), relating to executory contracts. Relying upon the fact that Section 1167 expressly exempted collective bargaining agreements subject to the Railway Labor Act, but granted no similar exemption to agreements subject to the National Labor Relations Act, the Court stated:

> Obviously, Congress knew how to draft an exclusion for collective bargaining agreements when it wanted to; its failure to do so in this instance indicates that Congress intended that Section 365(a) apply to all collective bargaining agreements covered by the NLRB.

Id. at 1195.

It must be presumed here that Congress knew how to draft an exclusion for governmental actions when it wanted to do so, as with the exception to the automatic stay under Section 362(a), 11 U.S.C. Section 362(a). The absence of a parallel exception in Section 554(a) is a clear indication of Congress' intent that the right to abandon not be subject to any exception for action by governmental

units. There is no indication in the language of Section 554(a) that any other conditions other than the "burdensome" and "inconsequential value" standards set forth in the statute should be applied.

As stated by District Court Judge Lacey in his opinion affirming the abandonment of the Long Island City facility, "reliance on Section 362 actually undercuts appellant's argument," (App.G, 60a), there being no comparable exception for governmental actions contained in Section 554 of the Code.

B. Restrictions upon the trustee's right to abandon pursuant to Section 554(a) based upon state law result in frustration of the full effectuation of the objectives of federal bankruptcy legislation and therefore violate the Supremacy Clause of the Constitution.

1. Courts cannot create categories of priorities or administrative expenses not recognized by the Bankruptcy Code.

Courts have consistently held that the original and primary purpose of bankruptcy legislation is the reduction of the debtor's property to money as expeditiously as practical, and a fair and equitable distribution of the property of the debtor to and among his creditors. States, by means of their own laws, cannot devise preferences among creditors of the debtor which the federal bankruptcy law does not recognize. *In re Universal Money Order Co.*, 470 F. Supp. 869 (S.D. N.Y. 1977); *In re Good Deal Supermarkets, Inc.*, 384 F. Supp. 87 (D. N.J. 1974).

The governmental authorities here are seeking to compel the trustee to retain and administer property which

is valueless and unprofitable, and to expend assets, which would otherwise be available for distribution to creditors, to maintain the property and dispose of the hazardous wastes located on the sites. In effect, the states are attempting to obtain a preference of one class of creditors over another, contrary to the express provisions and purposes of the Bankruptcy Code. The Supremacy Clause of Article VI of the Constitution demands that the conflict between the Bankruptcy Code and state legislation be resolved in favor of the Bankruptcy Code. Abandonment must be permitted.

Although the Court of Appeals recognized that "state law regulating the distribution of assets among creditors must give way to the all encompassing law of creditors' rights", 739 F. 2d at 920, the Court failed to recognize that, in effect, the denial of the trustee's right to abandon will result in a distribution of assets among creditors pursuant to state law rather than federal law. This result clearly is wrong, and frustrates the effectuation of the objectives of bankruptcy.

For the Court to say that the trustee must finance the cleanup would require a rearrangement of the priority of distribution not envisioned by the Bankruptcy Code. Secured and unsecured creditors would be required to pay for the cleanup of the facilities. The result would be to transfer the cost to parties who were in no way responsible for placing the contaminated oil on the sites. If the court insists that the cost of cleanup be borne by the innocent, then it is the innocent public which should carry that burden not a select innocent few. As noted by Judge Gibbons, the name of the state's game is:

> [T]ransferring the cost of cleanup to secured and unsecured creditors of the debtor, in this instance outside New York, who have no interest whatever in the Long Island City property, and who, on the record before us, were in no way responsible for placing the contaminated oil on that site.

In the Matter of Quanta Resources Corp., etc., supra at 925.

2. Under the circumstances of this case, a Trustee in Bankruptcy has no alternative but to refuse appointment or, once having accepted appointment, to resign.

Where is a trustee in bankruptcy left under the decision of the Court of Appeals? Does he remain the owner of the property forever? Which site must be cleaned first—New York or New Jersey? Can he be subject to criminal sanctions or personal liability for costs of cleanup? Can the estate never be closed? Can creditors be charged with the cost of cleanup and, if so, which creditors? These and many other important questions were left unanswered.

A perfect example of the frustration of the purposes of federal bankruptcy law which will result is found in the case of *In re Charles George Land Reclamation Trust*, 30 B.R. 918 (Bkrptcy D. Ma. 1983). The debtor in that case owned and operated a waste disposal facility. Prior to the filing of a bankruptcy petition, the debtor had entered into a consent judgment with the Commonwealth of Massachusetts requiring the debtor to undertake certain actions to bring the facility into compliance with environmental laws and regulations. The required remedial actions had not been completed as of the filing of the bankruptcy petition. The Commonwealth of Massachusetts

argued before the Bankruptcy Court that any trustee would have to immediately rectify the violations of law or otherwise find himself in violation of 28 U.S.C. Section 959(b). As a result, no private panel member would agree to serve as trustee. The United States Trustee, as a default trustee under 11 U.S.C. Section 15701(b), then brought an emergency motion for dismissal. This motion was granted.

To allow the decision of the Court of Appeals to stand would effectively preclude orderly liquidation of any debtor's estate where the debtor was under an obligation at the time of filing bankruptcy to take any remedial action under any other federal or state legislation. Nowhere in the Bankruptcy Code can there be found a legislative intent to deny such debtors the rights and protections under the Bankruptcy Code. Quite to the contrary, the Code evidences a congressional intent that claims of governmental units for environmental cleanup not be accorded priority or administrative expense status, but rather share with all other creditors in the distribution of the estate.

This Court's recent decision in *Ohio v. Kovacs*, supra, also stands for the proposition that an individual or other entity, which has engaged in business involving hazardous wastes or materials which may result in adverse environmental consequences, is not to be automatically denied the protections of the bankruptcy code.

C. Denial of the Trustee's right to abandon pursuant to Section 554(a) of the Bankruptcy Code is inconsistent with the decision of the Supreme Court in United States v. Security Industrial Bank, 459 U.S. 70 (1982), and is violative of the "takings clause" of the Fifth Amendment.

A substantial basis for Judge Gibbons' dissent was the decision of this Court in *United States v. Security Industrial Bank,* supra, where it was held that:

> The Bankruptcy Act should not be construed to destroy the interest of creditors when a substantial question arises as to whether the act constitutes a taking of property without just compensation.

In the Matter of Quanta Resources Corp., etc., supra at 924 (3rd Cir. 1984). Quoting from *Security Industrial Bank,* Judge Gibbons stated that the holding was a corollary of the longstanding doctrine that the Court is obligated:

> First (to) ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided . . . similarly, in the absence of a clear expression of Congress intent . . . (a court should) decline to construe the Act in a manner which could in turn call upon the Court to resolve difficult and sensitive questions arising out of the guarantees of the "takings clause". (Citations omitted).

Ibid.

The majority's construction of Section 554(a) raises a substantial question under the "takings clause" of the Fifth Amendment, U.S. Const., Amend. 5, since the requested cleanup of the properties would completely ex-

haust the assets of the estate, both secured and unsecured.[5] A construction of Section 554 of the Code is available, however, which would avoid this difficult constitutional question. Section 554(a) provides that:

> After notice and hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

11 U.S.C. Section 554(a). There is no question here but that the two facilities were burdensome to the estate and of inconsequential value to the estate.[6] Having satisfied this criteria, the plain language of Section 554(a) permits

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[5]The dissenting opinion contained the following discussion on this point:

The "taking" concern has been raised previously:

[T]he public interest cannot demand the erosion of the bankrupt's assets to the point of confiscating practically the entire estate. At some point the extent and degree of taking runs into the constitutional prohibition in the Fifth Amendment [on] the taking of private property for public use without just compensation.

In re New York, New Haven and Hartford Railroad Co., 330 F. Supp. 131, 147 (D. Conn. 1971); see also H.R. Rep. No. 595, 95th Cong. 1st Sess. 423 (1977), reprinted in 1978 U.S. Code Cong. & Ad. News, 5963, 6379:

Subsection (a) [11 U.S.C. Section 1170(a)] permits the court to authorize the abandonment of a railroad line if the abandonment is consistent with the public interest and either in the best interest of the estate or essential to the formulation of a plan . . . The authority to abandon or not to abandon lines of railroad is, of course, subject to the fifth amendment of the Constitution, which may in particular cases require abandonment in order not to erode a secured creditor's interest in the debtor's property even though the public interest dictates otherwise. *In the Matter of Quanta Resources Corp. etc.,* supra at 925.

[6]The majority held that "this factual finding is not challenged on appeal." 739 F.2d at 914, footnote 4.

abandonment in both cases, thereby avoiding the constitutional question under the "takings clause" of the Fifth Amendment.

Under the holding of *United States v. Security Industrial Bank,* supra, the Court must read Section 554(a) in such a manner as to avoid the constitutional question. Accordingly, Section 554(a) must be read as permitting abandonment under the facts of this case.

The Court should also be mindful of the potential consequences of a decision which would strip innocent lenders of all protection and require that their security be expended for a cleanup of the debtor's property. Such a result would immediately dry up all sources of financing for companies in any way engaged in the treatment or handling of hazardous materials or waste.

D. 28 U.S.C. Section 959(b) does not constitute a bar to abandonment by the Trustee.

1. 28 U.S.C. Section 959(b) is not applicable to a bankruptcy trustee in a liquidation proceeding.

Following a lengthy analysis of the provisions of 28 U.S.C. Section 959(b), the Court of Appeals admitted that Section 959(b) was "not itself an independent prohibition of the trustee's abandoning property in contravention of state law . . .", and that the scope of the section could be construed as limited to administration of the debtor's business as a going concern (739 F. 2d at 919). The Court further cited the interpretation of Section 959(b) found in Moore's:

> But Section 959(b) applies *only to the receiver in his operation of the property in his possession.* It does not apply to the distribution of the estate and does not require the federal receivership court to comply with state laws regulating the distribution of funds in receivership, although *Erie R. Co. v. Tompkins* should now require it to do so in cases involving only non-federal matters. (emphasis added)

7-Pt. 2 Moore's Federal Practice, ¶ 66.04[4] at 1913 (J. Moore & J. Lucas) 2d Ed. 1982. (footnotes omitted). Since Section 959(b) is not an independent bar to abandonment, can reasonably be construed as limited in scope to an ongoing business, and since the only cited authorities support this limitation, it is respectfully submitted that 28 U.S.C. Section 959(b) does not prohibit abandonment by the trustee.

2. Abandonment of property of the estate by a Trustee in Bankrutpcy in accordance with 11 U.S.C. Section 554(a) does not violate state laws or regulations.

At the heart of our disagreement with the majority is the Court's faulty premise that abandonment would be in contravention of state and local environmental protection laws. The Court of Appeals stated that the issue as to the New York site was:

> Does 11 U.S.C. Section 554 (1982) permit the abandonment of property of the bankrupt estate in contravention of state and local environmental protection laws?

739 F. 2d at 913. Again as to the New Jersey site, the Court stated that:

> [T]he trustee does not have the right to abandon property of the estate where abandonment contravenes state public health and safety laws, as it does here.

739 F. 2d at 929. This premise is factually wrong in that pre-petition actions of the debtor constituted the contra-

vention of environmental protection laws, and is legally incorrect in misconstruing the nature and effect of abandonment under the Bankruptcy Code. The trustee has taken no affirmative action as to the contaminated oil, and therefore cannot be said to be disposing of the oil in contravention of state and local laws. Abandonment cannot be equated to disposal.

The history and purpose of abandonment under the prior Bankruptcy Act and the present Bankruptcy Code indicate that the right has evolved from a "judge made rule" to a congressionally recognized power under the Bankruptcy Reform Act of 1978.[7] Discussing the background and legislative history of a trustee's right to abandon property of the estate, Collier states that:

> No provision, however, specifically dealt with the abandonment of burdensome property in liquidation cases. By analogy to the trustee's power to reject executory contracts, cases under prior law permitted the trustee to abandon property that was either worthless or overburdened or for any other reason when it was certain that the property would not yield any benefit to the general estate. This practice furthered the *paramount purpose of bankruptcy liquidation: the reduction of the debtor's property to money as expeditiously as practicable so as to secure funds for distribution to general creditors. Forcing a trustee to retain and administer property that was valueless or unprofitable is contrary to that purpose.* (emphasis added)

[7]As such, decisions under the prior Bankruptcy Act relied upon by the Court of Appeals are not persuasive authority. See *Ottenheimer v. Whitaker*, 198 F.2d 289 (4th Cir. 1952), affirming 102 F. Supp. 913 (D. Md. 1952), and *In re Lewis Jones*, 1 B.C.D. 277 (Bk. Ct. E.D. Pa. 1974).

4 *Collier on Bankruptcy,* Section 554.01 (15th Ed.) Collier goes on to state that:

> Former section 70a of the Act vested title to the debtor's property in the trustee. Abandonment then divested the trustee of this title and revested it in the debtor. Under Section 541, the Trustee no longer takes title to the debtor's property, and, upon abandonment under Section 554, the trustee is simply divested of control of the property because it is no longer part of the estate. Thus, abandonment constitutes a divestiture of all interests in the property that were property of the estate.

4 *Collier on Bankruptcy,* Section 554.02 (2) (15th Ed.)

When a trustee abandons property, the property stands as if no bankruptcy had been filed. The property reverts back to the debtor as of the date of the commencement of the proceedings. In effect, the debtor is treated as having owned it continuously. *Mason v. CIR,* 646 F.2d 1309 (9th Cir. 1980). Liens encumbering property abandoned by the trustees are not affected, and the debtor holds in the same manner as prior to the filing of the bankruptcy. *In re Tarpley,* 4 BR 1945 (Bkrptcy Ct. Tenn 1980). The Trustee is deemed to have never had title to or custody of the property.

Upon abandonment, the trustee here stands as if he never had an interest in either facility. He has neither taken any action nor refrained from taking any action that would subject him to liability under state or local laws. The suggestion that the trustee could be personally exposed to criminal sanctions solely by virtue of his appointment by a federal court to serve as a trustee in bankruptcy is proof of how the objectives of the Bankruptcy Code will be frustrated by the Court of Appeals' decision.

It would be a different matter, of course, if the trustee had actually operated the property in his possession, which post-petition operation resulted in violations of environmental laws. To equate the trustee's sole act of taking custody of the property between the date of his appointment and the date of the abandonment to a disposal of hazardous wastes in violation of federal, state and local environmental laws quite obviously is a strained interpretation of the concept of abandonment. There being no violation of law on the part of the trustee, the trustee cannot be denied the right to abandon assets of the estate based upon these laws. Rather, for the trustee not to abandon this property would be violative of his duties enumerated in 11 U.S.C. Section 704. See also *In re Harper,* 175 F. 412 (N.D.N.Y. 1910); *In re Zehner,* 193 F. 787 (A.D. La. 1912); *In re Watts,* 19 F.2d 526 (E.D. La. 1927); and *Bowman v. Towery,* 207 Okla. 4, 248 P. 2d 1030 (1952).

It appears that the Court overlooked the correct analysis of abandonment under the Bankruptcy Court in efforts to dramatize a confrontation between bankruptcy law and environmental safety.

E. The states are to be treated as general unsecured creditors having claims arising out of pre-petition conduct of the debtor.

1. The claims of New York and New Jersey are not entitled to priority or administrative expense status.

The question of the right of governmental units to priority or administrative expense status was addressed by Congress in connection with the enactment of the exception to the automatic stay provisions. 11 U.S.C. Section 362. The Congressional House Report Comments on Section 362 include the following:

> Paragraph (4) excepts commencement or continuation of actions and proceedings by governmental units to enforce police or regulatory powers. Thus, where a governmental unit is suing a debtor to prevent or stop violation of fraud, environmental protection, consumer protection, safety, or similar police or regulatory laws, or attempting to fix damages for violation of such a law, the action or proceeding is not stayed under the automatic stay.
>
> Paragraph (5) makes clear that the exception extends to permit an injunction and enforcement of an injunction, and to permit the entry of a money judgment, but *does not extend to permit enforcement of a money judgment.* Since the assets of the debtor are in the possession and control of the bankruptcy court and since they constitute a fund out of which all creditors are entitled to share, *enforcement by a governmental unit of a money judgment would give it preferential treatment to the detriment of all other creditors.* (emphasis added.)

H.R. Rep. No. 595, 95th Cong. First Sess. 343 (1977), reprinted, in (1978), U.S. Code Cong. & Ad. News 5963, 6299. The intent to deny priority or preferential treatment is clear.

As pointed out in the decision in *Charles George Land Reclamation Trust,* supra, Congress had an additional opportunity to consider the question of the priority of federal and state governmental claims for cost of cleaning up hazardous substances. A bill introduced by Rep. Florio on September 23, 1982 (H.R. 7172) would have given priority to such claims. The bill was defeated. The fact that it was necessary to introduce such a bill also in-

dicates that such priority is not accorded to these claims under the bankruptcy code.

New York and New Jersey further appear to seek a "super-priority" status for their claims such as that contemplated by 11 U.S.C. Section 364(c). Nowhere in the Bankruptcy Code can there be found an express or implied intent to accord such status to any claims other than those expressly set forth in the Code.

As to whether the claims of New York and New Jersey could be accorded administrative expense status under 11 U.S.C. Section 503(b)(1)(A), Judge Gibbons, in his dissenting opinion, characterized as "preposterous" the contention that the cleanup costs for assets which are of no value to the estate could be classified as "necessary costs and expenses of preserving the estate." 11 U.S.C. Section 503(b)(1)(A). While, as noted by the majority, the categories enumerated in Section 503 are not exclusive, it is clear that all categories relate to preservation of the estate. In no way will a cleanup of the properties benefit or preserve the estate. The only result can be the exhaustion of all assets of the estate, and the denial to all other creditors of the right to share in the distribution of the estate.

A recent Bankruptcy Court decision from the Northern District of Ohio does, however, accord administrative expense priority to a claim of the United States Environmental Protection Agency ("E.P.A.") for reimbursement under the Comprehensive Environmental, Response, Compensation and Liability Act of 1980 ("CERCLA"), 42 U.S.C. Section 9601, et seq., for reimbursement of costs incurred by EPA in removing hazardous material from a site operated by the debtor. *In re T. P. Long Chemical, Inc.*, 45 B.R. 278 (Bkrptcy N.D. Oh. 1985). While that case is factually distinguishable on several grounds,[8] the importance of the *Long* case for this case is the Court's handling of the claim for reimbursement of cleanup costs. While we believe that the Court's analysis of the trustee's right to abandon the property which relies in large measure upon *In the Matter of Quanta Resources Corp., etc.*, supra, is incorrect, we also believe that the Court erred in its reasoning on the question of priority.

The decision merely contains the following conclusory statement of the question of priority:

> Since the estate cannot avoid the liability imposed by CERCLA, it follows that the costs incurred by the EPA in discharging this liability is an actual necessary cost of preserving the estate entitled to administrative expense priority.

In re T. P. Long Chemical, Inc., supra at 286. The sole support for this proposition is the case of *In re Vermont Real Estate Inv. Trust*, 25 B.R. 84 (Bkrptcy Vt. 1982),

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[8]A. The claim was made the federal government under CERCLA;

B. The tank which was opened resulting in a release of the hazardous substance which prompted the cleanup by the EPA had been sold to a third party prior to the spill;

C. Other buried drums containing hazardous material were buried at the rear of the property unknown to anyone except the debtor himself;

D. The debtor as debtor-in-possession did operate the business at this site while the case was under Chapter 11;

E. The trustee did not take positive steps to abandon the property prior to the time EPA took its removal action;

F. There were sufficient assets in the estate to reimburse the EPA.

which was a Chapter 11 proceeding where the debtor leased certain real property. A part of the leasehold premises collapsed due to the weight of accumulated snow resulting in a dangerous condition. Upon the failure of the debtor to demolish the remainder of the collapsed building, the City of Montpelier proceeded with the work and asserted a lien against the leasehold premises for reimbursement of its $8,500.00 expenditure.

In according administrative expense status to the claim, the Court held that it was an actual, necessary cost and expense of preserving the estate. The Court noted that it was necessary for the preservation of the leasehold as part of the debtor's estate. *In re Vermont Real Estate Inv. Trust,* supra at 806.

We do not believe that the *Vermont* case stands as authority for the proposition that costs incurred for cleanup or removal of hazardous wastes, which costs in no way benefit the estate, are entitled to administrative expense status. While the Court in *In re T. P. Long Chemical, Inc.,* supra, may be correct in holding that EPA was entitled to a claim under CERCLA for the costs of removal, we believe that the Court erred in according the claim administrative expense priority.

In the context of reorganizations, it has been held that in order for a claim to be granted administrative priority, it must arise from a transaction with a debtor in possession and be beneficial to the debtor in possession in the operation of the business. *In re Mammoth Mart, Inc.,* 536 F.2d 950 (1st Cir. 1976); *Matter of Jartran, Inc.,* 732

F. 2d 584 (7th Cir. 1984). Extending this reasoning to the case of a trustee in liquidating an estate, administrative priorities should only be given to those expenses which arise from a transaction with the trustee which is beneficial to the trustee in liquidating the estate. Costs of remedying conditions existing at the time of the filing of the bankruptcy petition do not arise from a transaction with the Trustee nor, under the facts of this case, are they beneficial to the Trustee. Administrative expense status therefore is inappropriate for claims seeking redress for pre-bankruptcy acts of the debtor.

2. There exists no basis for subordination of administrative, secured, and other unsecured claims to the claims of New York and New Jersey.

What the state and local governmental units effectively seek here is a subordination of all other claims, whether secured, super-priority, administrative or unsecured, to their claims. New York seeks reimbursement of the $2.5 million it expended subsequent to the trustee's abandonment of the Long Island City site. New Jersey, not having spent any money, seeks to compel the Trustee to undertake removal of hazardous materials from the Edgewater, New Jersey site. In any event, the states want these claims to be paid first. New York, in seeking to reach assets of the debtor located in New Jersey, actually seeks more than its own statute permits.

Under Section 510 of the Bankruptcy Court, 11 U.S.C. Section 510, courts have jurisdiction to subordinate, on equitable grounds, all or any part of an allowed claim or interest to all or any part of another allowed claim or interest. Before the Bankruptcy Court will exercise its power of equitable subordination, however, three conditions must be satisfied:

(1) The claimant must have been engaged in some type of inequitable conduct;

(2) The misconduct must have resulted in injury to creditors of the bankrupt or conferred an unfair advantage on the claimant, and

(3) Equitable subordination of the claim must not be inconsistent with the provisions of the Bankruptcy Act. *Matter of Mobil Steel Company,* 563 F. 2d 692, 700 (5th Cir. 1977); *In re American Lumber Company,* 5 B.R. 470 (D.C. Minn. 1980). The fundamental aim of subordination is to undo or to offset any inequity in the claim position of a creditor that will produce injustice or unfairness to other creditors in terms of the bankruptcy result. *In re Kansas City Journal-Post Co.,* supra; *In re Westgate-California Corp.,* 642 F. 2d 1174 (9th Cir. 1981). Generally, the claim will not be subordinated unless it is shown that the claimant has acted inequitably in the course of his relationship with the debtor and that those activities have harmed the debtor or his other creditors in some way.

In re Ahlswede, 516 F. 2d 784, 788 (9th Cir. 1971); *In re Westgate-California,* supra.

There has been no allegation, and there exists no basis for any allegation, that the Trustee or any other creditor engaged in any inequitable conduct or misconduct which harmed the debtor or respondents. There is no basis in the Bankruptcy Code or case law for subordination of any claims to the claims of New York and New Jersey.

F. Under the circumstances of this case there is no irreconcilable conflict between the Bankruptcy Code and environmental protection.

Abandonment here actually serves to accommodate state environmental laws rather than to abrogate the enforcement of these laws. Abandonment would represent no additional environmental destruction; it would merely leave unrepaired past misconduct for which the states have pre-petition claims.

The Code itself effects a reasonable accommodation between regulatory enforcement and the protection of the debtor and the estate in bankruptcy. Governmental authorities are unimpeded in requiring that a debtor's ongoing conduct comply with environmental or other regulations. When they seek to remedy pre-bankruptcy violations, however, they are limited to collecting their allotted

share of the estate in bankruptcy and invoking any available exceptions to discharge, thus preserving both the respective shares of other creditors and the fresh financial start provided the debtor by the discharge.

Upon the failure of a landowner to implement cleanup measures, both the New York and the New Jersey statutes relied upon by respondents below are similar in result. If the state undertakes cleanup of the property and disposes of the hazardous waste, the state then becomes entitled to a lien.[9] By way of example, the New Jersey Spill Compensation and Control Act, N.J.S.A. 58:10-23.11, *et seq.* creates:

[9]The City of New York filed a Proof of Claim on October 7, 1982, in the sum of "approximately $5,000,000.00". The City claimed a lien pursuant to New York City Administrative Code Section 564.245 upon the Long Island City premises "for all expenses incurred by the City of New York in securing, removing and properly disposing the materials unlawfully placed there by the debtor."

The New York State Department of Environmental Conservation filed a Proof of Claim on July 14, 1982 in an amount "to be determined". The claim states that the cost of removal and disposal of waste oil and other hazardous substances constitutes its claim. New York State also claimed a first lien on the Long Island City property.

The Proof of Claim of the New Jersey Department of Environmental Protection, filed July 20, 1982, asserts that it is a "claim for an administrative expense of the estate which should be given priority over all secured claims of the estate". New Jersey further claimed "that all money received by the Trustee from the sale of oil or equipment at the facility in Edgewater should be applied toward the proper closure and cleanup of the facility".

> A first priority claim and lien paramount to all other claims and liens upon the revenues and all real and personal property of the discharger, whether or not the discharger is insolvent.

N.J.S.A. 58:10-23.11f. The claim and liens arise upon any expenditure by the administrator of the New Jersey Spill Compensation Fund.[10]

In this case, the City and State of New York, upon abandonment by the Trustee, received exactly what they claim they are entitled to, a lien on the New York property of the debtor. New Jersey, not having made any expenditures, was not entitled to a lien. If and when New Jersey does expend money, it will be free to pursue its remedies against the real property in Edgewater, New Jersey.

The states are free to direct future conduct of debtors and debtors-in-possession, but enforcement addressed to past regulatory violations necessarily takes the form of submitting a claim for allowance in bankruptcy and receiving whatever is paid in a distribution governed by the Code's priorities. See Hennigan, *Accommodating Regulatory Enforcement and Bankruptcy Protection,* 59 Am. Bankr. L. J. 1 (1985).

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[10]The Act was amended effective January 25, 1985, to limit the so-called "super-lien" to the property for which the expenditure was made.

CONCLUSION

In a footnote to the most recent decision involving the Bankruptcy Code and state environmental regulation, this Court described a situation factually identical to the case presently before the Court:

> Had no receiver been appointed prior to Kovacs' bankruptcy, the trustee would have been charged with the duty of collecting Kovacs' nonexempt property and administering it. If the site at issue were Kovacs' property, the trustee would shortly determine whether it was of value to the estate. If the property was worth more than the cost of bringing it into compliance with state law, the trustee would undoubtedly sell it for its net value and the buyer would clean up the property, in which event whatever obligation Kovacs might have had to clean up the property would have been satisfied. If the property were worth less than the cost of cleanup, the trustee would likely abandon it to its prior owner, who would have to comply with the state environmental law to the extent of his or its ability.

Ohio v. Kovacs, supra at 711.

This is precisely the situation here. No receiver was appointed prior to Quanta's bankruptcy. The trustee therefore was charged with the duty of collecting Quanta's nonexempt property and administering it. The Trustee made the determination, which has not been disputed, that the New York and New Jersey sites were of no value to the estate. The properties were not worth more than the cost of bringing them into compliance with state law. There were no prospective buyers willing to assume the responsibility to clean up the sites. The trustee was justified in seeking, under Section 554(a), and required, under Section 704, to abandon the property. The obligation for

cleanup then devolved upon the parties having a possessory interest in the property.

To hold otherwise would conflict with this Court's construction of the Bankruptcy Code and run afoul of the Supremacy Clause and Fifth Amendment to the Constitution.

In the concurring opinion in *Kovacs,* Justice O'Connor expressed the view that the Court's holding could not be viewed as hostile to state enforcement of environmental law. 105 S. Ct. at 712. Here too, abandonment by the trustee is not hostile to the states' rights to assert their entitlement to liens against the abandoned property, whether under federal or corresponding state law, or to pursue claims for reimbursement against the estate. Abandonment by the trustee permits the states to proceed with any necessary cleanup and pursue their available remedies under state law free from any requirement of obtaining permission from the Bankruptcy Court. Abandonment additionally removes the property from the custody of the trustee, who was powerless to do anything to correct the hazardous conditions or to protect the public against the potential hazards. Abandonment insured that the necessary remedial action could proceed expeditiously.

Environmental policy surely would not be advanced by leaving the hazardous sites in the control of a bankruptcy trustee who was unable even to maintain security. If the unlikely situation arose that a bankruptcy trustee had assets sufficient to undertake a cleanup, which cleanup in turn would produce a return to the estate upon sale of the cleaned up site in excess of the cost of the cleanup, this would be an entirely different matter. Under the

circumstances of this case, environmental policy is best served by removing the trustee from the picture and allowing the states to take appropriate action. A denial of abandonment would have only served to impede and needlessly delay the cleanup efforts by the states. Leaving the trustee in possession would have undercut the ability of the governmental entities to promote "public health and safety".

Based upon the foregoing it is respectfully submitted that the decisions of the United States Court of Appeals for the Third Circuit be reversed.

Respectfully submitted,

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(8) (9)

Nos. 84-801 and 84-805

In The

Supreme Court of the United States

October Term 1984

MIDLANTIC NATIONAL BANK,
Petitioner (No. 84-801),

vs.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondent,

and

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner (No. 84-805),

vs.

THE CITY OF NEW YORK and STATE OF NEW YORK, et al.,
Respondents.

On Writs of Certiorari to the United States Court of Appeals For the Third Circuit

BRIEF OF RESPONDENT NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION

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PETITIONS FOR CERTIORARI FILED NOVEMBER 14, 1984
CERTIORARI GRANTED AND CASES CONSOLIDATED FEBRUARY 19, 1985.

QUESTION PRESENTED

Whether the United States Court of Appeals for the Third Circuit correctly held that abandonment of PCB-contaminated waste oil was inappropriate under the Bankruptcy Code, 11 *U.S.C.* § 554(a), when abandonment by the trustee in a liquidation proceeding would violate state environmental laws and threaten the public safety?

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Respondent,

and

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner (No. 84-805),
vs.
THE CITY OF NEW YORK and STATE OF NEW YORK, et al.,
Respondents.

On Writs of Certiorari to the United States Court of Appeals For the Third Circuit

BRIEF OF RESPONDENT NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION

STATEMENT OF THE CASE

At issue in these consolidated cases is whether a trustee in bankruptcy may abandon property of an estate under 11 *U.S.C.* § 554(a)* when abandonment would per-

* 11 *U.S.C.* § 554(a) provides that, "After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value and benefit to the estate."

petuate a public nuisance, violate state and federal environmental laws, and threaten the public health, safety, and welfare. Both cases involve property contaminated with polychlorinated biphenyls (PCB's) that became part of the estate of Quanta Resources Corporation when that company filed a bankruptcy petition in October 1981. In the New Jersey case which will be the focus of this brief, the United States Bankruptcy Court for the District of New Jersey held, over the objection of the New Jersey Department of Environmental Protection ("NJDEP"), that abandonment of the contaminated property by the trustee was appropriate under 11 *U.S.C.* § 554(a) because the property was burdensome and of no value to the estate. A similar decision had previously been rendered in the New York case by the same Bankruptcy Court and was affirmed by the United States District Court for the District of New Jersey. Appeals in both cases were reviewed by the United States Court of Appeals for the Third Circuit, which reversed the holding below. In reversing, the Third Circuit held that abandonment was not justified in either case due to the serious risk to the public and the environment that would result. Petitions for *certiorari* from these holdings were filed by Thomas J. O'Neill, trustee in bankruptcy of Quanta, and by Midlantic National Bank ("Midlantic"), a creditor of Quanta with a security interest in some personal property of the estate. This Court granted *certiorari* and consolidated the cases on February 19, 1985. This brief, submitted on behalf of NJDEP, addresses the issue of abandonment in the context of the facts and State laws pertinent to the New Jersey case.

Quanta Resources Corporation leased a site along the Hudson River in Edgewater, New Jersey, at which it

operated a facility for the processing of waste oil and oil sludge. Quanta began operating at the site in mid-1980 when it purchased Edgewater Terminals, Inc., which had previously conducted a waste oil business at the same location. The waste oil industry in New Jersey is regulated by NJDEP under the Solid Waste Management Act, *N.J.S.A.* 13:1E-1 *et seq.* Pursuant to the regulatory scheme established under this State statute, Edgewater Terminals, Inc., had obtained a temporary operating authorization ("TOA") from NJDEP which allowed the facility to accept waste oil and sludges, but specifically prohibited the acceptance of PCB's (R. 11-12).*

Shortly after Quanta's assumption of operations at the Edgewater site, NJDEP entered into an Administrative Consent Order with Quanta in which the company agreed to apply for a TOA in its own name. This Order, dated August 6, 1980, also cited the facility for leaks and poor maintenance, and directed Quanta to remedy these serious deficiencies. Pending approval of this application, Quanta agreed to conduct its operations in accord with the TOA issued to Edgewater Terminals, Inc. (R. 13 to 22.)

On May 29, 1981, NJDEP issued a TOA to Quanta in conjunction with another Administrative Consent Order. This Order directed Quanta to remove all sludges from the site, to improve maintenance procedures, and to rectify the "chronic spills and leaks" that were occurring at

* Pertinent documents from the record in this case were included in the appendix filed with the United States Court of Appeals for the Third Circuit. "R" as used in this brief refers to that appendix.

the facility. NJDEP made the operation of the TOA contingent upon Quanta's satisfaction of the Department's demand for the improvement of environmental conditions at the site (R.22-24). In addition, the TOA expressly provided that, "[t]his facility is *not* authorized to accept PCB waste . . ." (emphasis in original) (R.25-37,34).

Less than one month after the issuance of this TOA, however, NJDEP investigators tested Quanta's tanks and discovered significant PCB-contamination. NJDEP then directed Quanta to cease operations at the Edgewater facility, which Quanta did on July 2, 1981. Although Quanta had represented to NJDEP that the company was interested in resolving the environmental problems at the facility, negotiations through the end of September 1981 proved inconclusive. Consequently, on October 7, 1981, NJDEP issued an Administrative Order to Quanta formally revoking its TOA and directing the company to prepare and execute a closure plan for the facility. This Order required Quanta to remove all hazardous waste in the closure process, including all material contaminated with PCB's (R.42-45). Quanta never complied with this Order.

On October 6, 1981, however, Quanta filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code. Quanta remained in possession of the property of the estate as debtor-in-possession until November 11, 1981. At that time the reorganization was converted to a Chapter 7 liquidation and Thomas J. O'Neill took control of the estate as trustee in bankruptcy.

The estate consisted of non-New Jersey real property, a leasehold in the Edgewater facility, various equipment,

and oil, some of it contaminated and of no value, and some able to be sold. On April 5, 1982, Midlantic, which had a prebankruptcy security interest in all inventory and equipment of the debtor, obtained an order from the Bankruptcy Court establishing the extent and amount of Midlantic's lien: $643,660.68 plus interest from October 6, 1981.

On August 24, 1982 an order was entered by the Bankruptcy Court approving the sale by the trustee of all equipment and vehicles of the estate for $315,145, which after deducting for liens on the vehicles and the cost of the sale, realized just over $200,000 for the estate.

In October 1982, the trustee filed the first of a series of notices proposing to abandon approximately 1,600,000 gallons of mixed industrial and automotive waste oil that were located at Quanta's facility in Edgewater. According to this notice, approximately half of this oil was contaminated with PCB's and hence was not saleable, while the remainder was subject to an offer of sale previously approved by the Bankruptcy Court but not executed (R.4). NJDEP opposed the abandonment, filing papers to this effect (R.5-10). At the time of the proposed abandonment, the facility was "in an extreme state of disrepair." Affidavit of Frank Gagliano, Senior Environmental Specialist at NJDEP, dated September 27, 1982 (R.45-48, at 45). Many of the tanks were leaking, the oil-water separator—a critical pollution control device—was not working, and seepage of waste oil into the Hudson River was occurring. Tank ruptures resulting in large spills of contaminated oil into the River were feared (R.46).

Despite the ongoing environmental problems at the Quanta facility and the attendant risks to the public health

and safety, and despite the objections of NJDEP, the United States Bankruptcy Court for the District of New Jersey issued an order authorizing the abandonment of the contaminated oil on May 20, 1983 (R.1-2, also included in Appendix I attached to the petition for *certiorari* filed by Thomas J. O'Neill, trustee in bankruptcy). The Order also authorized the trustee to abandon Quanta's leasehold interest in the Edgewater site and any personal property of the debtor still located at the facility. The Order directed the trustee to retain possession of the non-contaminated oil, however, pending its sale.

On June 21, 1983, the Trustee completed the sale of the noncontaminated oil for $257,494.14. The net proceeds to the estate, after costs of sale, were approximately $200,000. By consent of the trustee, NJDEP, Midlantic and the New Jersey landlords, the proceeds of the sale were distributed to Midlantic without prejudice to the right of NJDEP to recover from all parties such funds of the estate, including the proceeds of the oil sale, as NJDEP might gain entitlement to through further prosecution of the case.

Thereafter, upon the consent of the parties, NJDEP filed a direct appeal of the order of the Bankruptcy Court authorizing abandonment to the United States Court of Appeals for the Third Circuit pursuant to 28 *U.S.C.* § 1293(b) (R.48-49). In two companion decisions issued on July 20, 1984, *Matter of Quanta Resources Corp.*, 739 *F.*2d 912 (3d Cir. 1984) (New York case), and *In re Quanta Resources Corp.*, 739 *F.*2d 927 (3d Cir. 1984) (New Jersey case), the Third Circuit held that the trustee in bankruptcy could not abandon contaminated property in the Quanta estate as long as that property constituted a

threat to the public health and safety. In this regard the court stated that:

> If trustees in bankruptcy are to be permitted to dispose of hazardous wastes under the cloak of the abandonment power, compliance with environmental protection laws will be transformed into governmental cleanup by default. It cannot be said that the bankruptcy laws were intended to work such a radical change in the nature of local public health and safety regulation—the substitution of governmental action for citizen compliance — without an indication that Congress so intended. [739 *F.*2d at 921-922 (footnote omitted).]

To reach this holding, the Third Circuit analyzed the relationship between State environmental laws and the abandonment power created by Congress in 11 *U.S.C.* § 554. It found in this regard that § 554 did not preempt State police power regulation and that, in fact, the judge-made law upon which § 554 was based had itself prohibited abandonment where such an action would endanger the public health and safety, citing ***Ottenheimer v. Whitaker***, 198 *F.*2d 289 (4th Cir. 1952), and ***In re Lewis Jones, Inc.***, 1 Bankr. Ct. Dec. (CRR) 277 (Bankr. E.D. Pa. 1974). Furthermore, the Third Circuit found evidence of Congressional intent to defer to State police power regulation of a business involved in bankruptcy proceedings in 11 *U.S.C.* § 362(b)(4) (exception to automatic stay of actions against debtor for the enforcement of a governmental unit's police or regulatory power), and 28 *U.S.C.* § 959(b) (requiring a trustee to manage and operate property in his possession according to the laws of the State in which the property is situated). The court also relied upon the equitable powers vested in the Bankruptcy Court in 28 *U.S.C.* § 1401, and the fact that the equities in this case

favored protection of the public safety over preservation of the estate for the benefit of creditors, to support its decision that abandonment of the contaminated property was improper. Finally, the court below expressly declined to reach the issue of who should pay for the clean-up of the Edgewater facility. 739 *F.*2d at 929.

Both the trustee in bankruptcy of the Quanta estate and Midlantic National Bank, a creditor of Quanta's New Jersey property, filed petitions for *certiorari* in this Court from the decisions of the Third Circuit. These petitions were granted, and the New York and New Jersey cases were consolidated, on February 19, 1985. Since that time the United States Environmental Protection Agency ("EPA") has undertaken immediate and planned removal actions at the Quanta site in Edgewater pursuant to the Comprehensive Environmental Response, Compensation and Liability Act ("CERCLA"), 42 *U.S.C.* § 9601 *et seq.,* and 40 *C.F.R.* 300.65 to 300.67. In this regard, NJDEP has entered into a cooperative agreement with EPA in which the State has agreed to pay ten percent of the cost of the planned removal. Although the purpose of these cleanup actions is to stabilize the site and prevent further pollution of the Hudson River and the property surrounding the facility, this governmental action is of an emergency nature and will not completely remedy the environmental problems at the site.

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SUMMARY OF ARGUMENT

The power of a trustee in bankruptcy to abandon property burdensome to the estate was codified in 11 *U.S.C.* § 554 which brought the previously judge-made law of abandonment into the Bankruptcy Code for the first time. 4 *Collier on Bankruptcy* § 554.01, at 554-2 (15th ed. 1985). Since prior law had established that the exercise of the abandonment power was not absolute, but rather was subject to police power regulations and could be denied in the public interest — *Ottenheimer v. Whitaker,* 198 *F.*2d 289 (4th Cir. 1952); *In re Lewis Jones, Inc.,* 1 Bankr. Ct. Dec. (CRR) 277 (Bankr. E.D. Pa. 1974); 4A *Collier on Bankruptcy* § 70.42[2] at 502-504 (14th ed. 1978)—the codification of the abandonment power implicitly incorporated this important limitation. For, where Congress adopts legislation containing terms and concepts that have previously accumulated meaning under equity or the common law, a court should infer from such use that Congress intended to incorporate the established meaning into the statute. *NLRB v. Amax Coal Co.,* 453 *U.S.* 322, 329 (1981).

The "public safety" exception to the abandonment power should be applied in this case because the property sought to be abandoned by the trustee constituted a continuing health and environmental threat in that it was contaminated with PCB's, was leaking onto the ground and into the Hudson River and, due to poor maintenance, was so unstable that a major spill was likely unless preventive measures were taken. The poor condition of the property also constituted a public nuisance in ongoing violation of State and federal laws such as the Spill Compensation and Control Act, *N.J.S.A.* 58:10-23.11a *et seq.,*

the Solid Waste Management Act, *N.J.S.A.* 13:1E-1 *et seq.*, CERCLA, 42 *U.S.C.* § 9601 *et seq.*, and the Toxic Substances Control Act, 15 *U.S.C.* § 2601 *et seq.* Since abandonment would remove control of the property from the trustee, who had some assets available that could have been used for stabilization and other remedial activities, and would return the property to the assetless corporate shell of the debtor, such action would further endanger the public safety and violate State and federal environmental laws. Under such circumstances, abandonment cannot be condoned.

Since Congress implicitly incorporated the public safety exception to abandonment in 11 *U.S.C.* § 554, there is no real issue of federal preemption of State police powers in this case. If there were, however, Congress has demonstrated in 11 *U.S.C.* § 362(b)(4) (exception to automatic stay for police power enforcement actions and 28 *U.S.C.* § 959(b) (requirement that trustee manage property in his possession in accord with State laws), that it did not intend the Bankruptcy Code to abrogate a State's police powers or exempt trustees from complying with State law. Moreover, since the New Jersey statutes in question here have federal counterparts with overlapping goals, the bankruptcy and environmental laws should be read in harmony, giving effect to both. *See Ruckelshaus v. Monsanto Co.*, 104 *S.Ct.* 2862, 2881 (1984).

The sole issue addressed below was the propriety of abandonment when the public health and safety are at risk. The Third Circuit expressly refused to reach the issue of entitlement or priority access to the assets of the estate. The "taking" challenge raised by petitioners is thus premature. If it is entertained, however, the challenge should be rejected because it was the illegal acts of the polluter that diminished the value of the creditors' collateral or interest, and not the regulatory activities of the State government undertaken to protect the public. Neither the Constitution nor the Bankruptcy Code requires States to indemnify creditors for poor investments or bad business decisions.

ARGUMENT

POINT I

THE COURT BELOW CORRECTLY INTERPRETED AND APPLIED 11 U.S.C. § 554 TO PROHIBIT THE ABANDONMENT OF PROPERTY BY A TRUSTEE IN BANKRUPTCY WHEN SUCH ABANDONMENT WOULD ENDANGER THE PUBLIC SAFETY.

The United States Court of Appeals for the Third Circuit held in its decision in this matter that Congress incorporated the judge-made law of abandonment into 11 *U.S.C.* § 554, thus including in that statutory provision the judge-made restriction that prevents abandonment when such action would place the public at risk and violate laws of a police power nature. The Court below then went on to apply this public safety exception to the facts of this case, concluding that the abandonment of PCB-contaminated waste oil by the trustee would unduly endanger the public and the environment and would consequently be improper. NJDEP submits that these holdings were correct and must be affirmed.

A. In Enacting 11 U.S.C. § 554, Congress Codified The Pre-Existing Judicially-Formulated Rule That Authorized Abandonment Only When It Would Be Consistent With Police Power Statutes And The Public Interest.

The Bankruptcy Act of 1899 contained no abandonment provision. Instead, the principles governing abandonment of property of the estate developed through judicial rulings. *See, e.g., In re Chicago Rapid Transit,* 129 *F.*2d 1, 4 (7th Cir.), *cert. den.* 317 *U.S.* 683 (1942). The early drafts of legislation that evolved into the Bankruptcy Reform Act of 1978 directly incorporated the concept of abandonment into the statutory scheme. Section 4-611 of the proposed Bankruptcy Act of 1973, submitted by the Congressionally-established Commission on the Bankruptcy Laws of the United States, and introduced into Congress as H.R. 10792, 93rd Cong., 1st Sess. (1973), provided:

> The trustee may, subject to the approval of the administrator, abandon to the debtor any property of the estate if it is burdensome or has no net realizable value. Abandonment may be without notice, hearing, or order of the court, but until 10 days after entry of a notation of the abandonment in the file of the case, the abandonment is subject to contest on a complaint filed by a party in interest any time during the pendency of the case.

The Note to Section 4-611 reads in pertinent part: "This section is new but is adapted from Proposed Rule 608. The concept of abandonment is well recognized in the case law. See 4A Collier § 70.42[3] (1967)." This early legislative statement provides an indication of Congress' intent to codify the existing case law on abandonment.* *See* "Analysis of the Bankruptcy Reform Act of 1978," 1979 *Annual Survey of Bankruptcy Law* 322 (W. Norton, ed.).

This pre-Code case law clearly indicates that the trustee's right to abandon burdensome property was not absolute and superior to the requirements of other federal and state laws. In discussing a trustee's right to abandon burdensome property prior to the enactment of 11 *U.S.C.* § 554, *Collier on Bankruptcy* stated that although a trustee "may abandon any property which is either worthless, or overburdened, or for any other reason certain not to yield any benefit to the general estate . . . [r]ecent cases illustrate, however, that the trustee in the exercise of the power to abandon is subject to the application of general regulations of a police nature." 4A *Collier on Bankruptcy* § 70.42(2) (14th ed.) (footnote omitted).

Several pre-Code cases established this restriction on the trustee's right to abandon worthless or burdensome property. *Ottenheimer v. Whitaker,* 198 *F.*2d 289 (4th Cir. 1952), involved facts and issues analogous to those at bar. In *Ottenheimer,* the trustee in bankruptcy petitioned the court for leave to abandon certain floating barges that were burdensome to the estate. The abandonment was opposed by the Harbor Engineer of the City of Baltimore and the United States Army Corps of Engineers on the ground that the proposed abandonment would

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* It should be noted that the only differences between proposed Section 4-611 and Section 554 are procedural in nature. The standards for abandonment contained in the two provisions are nearly identical.

violate 33 *U.S.C.* § 409, which made it unlawful to sink voluntarily or cause to be sunk vessels in navigable channels. In addition, the barges were in a dilapidated and unsafe condition and would sink at anchorage if abandoned. The court not only denied the trustee permission to abandon the barges, but directed him to remove them from the anchorage and mandated that the cost of removal be borne by the bankrupt estate as a cost of administration. The court also pointed out that the general rule permitting a trustee to refuse acceptance of property of an onerous or unprofitable nature would have applied were it not for the unusual consequences that would follow:

> There can be no doubt that the property not only has no value, but also that the care and disposition of it will involve the expenditure of a substantial sum of money. But it is equally true that if the trustee abandons the barges and at the same time holds on to the valuable assets of the estate, the title to the barges will revert to the bankrupt and he will be left without means to care for or dispose of them in the manner prescribed by the statute. [198 *F.*2d at 290]

The court went on to emphasize that what was at issue was not "a burden imposed upon the bankrupt or his property by contract, but a duty and a burden imposed upon an owner of vessels by an Act of Congress in the public interest." *Ibid.*

The Bankruptcy Court for the Eastern District of Pennsylvania reached a similar result in *In re Lewis Jones, Inc.*, 1 *Bkr. Ct. Dec.* (CRR) 277 (Bankr. E.D. Pa. 1974). In that case, the trustees of three bankrupt utility companies sought instruction from the court concerning

certain underground manholes, vents and steam pipes that could become hazardous to public health and safety if abandoned in their existing condition. These structures could be made safe by repaving, filling and sealing, but only at a very substantial cost. Interestingly, in *Lewis Jones,* no federal or state statute would have been violated had the trustees not spent the money to remove the potential hazard. Nevertheless, and despite the cost involved for the estate, the court ordered the trustees to remedy the potentially hazardous conditions.

When 11 *U.S.C.* § 554 was enacted, therefore, the public safety exception to the abandonment power was well established in the case law. Since Congress was essentially incorporating existing abandonment law into the Bankruptcy Code through § 554 (*see* note to § 4-611 of H.R. 10792, 93rd Cong., 1st Sess. (1973), cited above, and 4 *Collier on Bankruptcy* § 554.01, at 554-2 (15th ed. 1985)), Congress implicitly included the public safety exception in the abandonment provision as well. Although the legislative history of § 554 is silent on this point, such silence is "eloquent" because had Congress contemplated changing existing law, it would have made a statement to this effect. *See Edmonds v. Compagnie Generale Transatlantique,* 443 *U.S.* 256, 266 (1979) (Court interpreted federal maritime enactment as not upsetting well-established, judge-made rule of admiralty law); *Palmer v. Massachusetts,* 308 *U.S.* 79, 85 (1939) ("If this old and familiar power of the states [to regulate local railroad service] was withdrawn when Congress gave district courts bankruptcy powers over railroads, we ought to find language fitting for so drastic a change."). *Accord, NLRB v. Amax Coal Co.,* 453 *U.S.* 322, 329 (1981). In

fact, statutes should be read with a presumption favoring the retention of familiar principles, except where an explicit intent to the contrary is evident. *Ibid.; Isbrandtsen Co. v. Johnson,* 343 *U.S.* 779, 783 (1952). Moreover, when the issue raised is whether a given statutory provision is intended to abrogate traditional, well-established governmental as opposed to private rights, the presumption against such a construction of the statute is particularly strong. *United States v. Tilleraas,* 709 *F.*2d 1088, 1092 (6th Cir. 1983). These precedents counsel affirmance of the conclusion reached below that Congress did not intend to alter judge-made law in adopting 11 *U.S.C.* § 554, but rather incorporated the preexisting law, including the public safety exception, into the recent codification of the abandonment power.

B. The Abandonment Of PCB-Contaminated Waste Oil By The Trustee In This Case Was Improper Because Such Abandonment Violated State And Federal Law And Threatened The Public Health And The Environment.

When the trustee proposed to abandon the PCB-contaminated waste oil at the Quanta facility in Edgewater, New Jersey, the oil was leaking from poorly maintained tanks onto the ground and into the Hudson River. The undisputed evidence before the Bankruptcy Court established that pollution control equipment was inoperative, and that conditions at the facility were so poor that tank ruptures resulting in large spills to the River were feared. Affidavit of Frank Gagliano, Senior Environmental Specialist, NJDEP (R.45-47). Although the trustee had had control of Quanta's property and assets from November

1981 through October 1982 when abandonment of the waste oil was first proposed, he had not stabilized the tanks, stopped the leaks, or performed any other remedial measures. Rather than acting to address the environmental threat at the site, the trustee simply sought to abandon the contaminated oil, presumably to the assetless debtor. (Abandonment is to the debtor, or to any other person with a possessory interest in the property; *see* 11 *U.S.C.* § 541 and S. Rep. No. 989, 95th Cong., 2d Sess. 93 (1978), *reprinted in* 1978 U.S. Code Cong. & Admin. News 5787, 5878.) In effect, therefore, abandonment under these circumstances would constitute the improper disposal of the hazardous wastes.

Such disposal, and the perpetuation of the poor storage conditions at the facility, violated New Jersey's Solid Waste Management Act which governs the storage, treatment, processing, and final disposal of waste materials (including waste oil) in the State, and prohibits the kind of improper storage and disposal that occurred at the Quanta facility. *N.J.S.A.* 13:1E-1 *et seq.; see also N.J.A.C.* 7:26-1 *et seq.* Similarly, the abandonment of the PCB-contaminated waste oil contravened the federal Toxic Substances Control Act ("TSCA"), 15 *U.S.C.* § 2601 *et seq.,* which closely regulates the use, storage, and disposal of PCB's. *See* 40 *C.F.R.* § 761.3 which defines "disposal" broadly to include actions terminating the useful life of PCB items, and actions relating to the containment or confinement of PCB items. Under TSCA, the disposal of PCB items is prohibited except in specifically designated incinerators or in secured chemical waste landfills. 15 *U.S.C.* § 2605(e).

Since the trustee's abandonment of the contaminated oil to the assetless debtor resulted in continued deterioration of the tanks and the continued leaking and spilling of hazardous substances into the waters of the State, this action also constituted a violation of New Jersey's Spill Compensation and Control Act, *N.J.S.A.* 58:10-23.11a *et seq.* This statute prohibits the discharge of hazardous substances and defines "discharge" broadly as "any intentional or unintentional action or omission resulting in the releasing, spilling, leaking, pumping, pouring, emitting, emptying or dumping of hazardous substance into the waters of the State or onto lands from which it might flow or drain into said waters. . . ." *N.J.S.A.* 58:10-23.11b(h). The New Jersey Water Pollution Control Act, *N.J.S.A.* 58:10A-1 *et seq.* also prohibits discharges of pollutants into the waters of the State except in conformity with a valid permit. Similarly, "releases" of hazardous substances into the environment are prohibited under federal law by CERCLA, 42 *U.S.C.* § 9601 *et seq.*

Petitioners argue, however, that abandonment of hazardous wastes by the trustee would not violate any State or federal environmental law because when a trustee abandons property, title to the abandoned property revests in the debtor as of the date of the commencement of the bankruptcy proceedings. Petitioners fail to recognize, however, that this reversion applies only to the property's title. *Mason v. Commissioner of Internal Revenue*, 646 *F.*2d 1309, 1310 (9th Cir. 1980) ("the title reverts to the bankrupt, *nunc pro tunc.*"). In this case, the trustee of the estate is required to comply with the environmental laws at issue because of his control and possession of

property of the estate, not because he has title to the property. *See Ohio v. Kovacs*, 105 *S.Ct.* 705, 711-712 (1985). As a result, although the debtor may be treated as having had continuous title to the property that is abandoned by the trustee, this legal doctrine does not free the trustee from a duty to comply with environmental laws. *Ibid.* This doctrine of continuous title should not be expanded to encompass reversion of possession and control of property of the estate as of the date of the bankruptcy petition. The doctrine is but a legal fiction and should apply only if it achieves a just result. *Wallace v. Lawrence Warehouse Co.*, 338 *F.*2d 392, 394 n.1 (9th Cir. 1964). Since application of this legal fiction here would frustrate rather than promote a just result, and would undermine this Court's observation in *Kovacs* that a trustee in liquidation must comply with valid state environmental laws, 105 *S.Ct.* at 711-712, it is clear that expansion of this legal fiction must be rejected.

Although abandonment of the contaminated oil by the trustee violates the State and federal laws noted above, the trustee would be liable to ensure compliance with these enactments only in his capacity as the representative of the estate. 11 *U.S.C.* §323. Absent malfeasance by the trustee (which is not alleged here), there would be no personal liability for the trustee under the environmental laws in this case, therefore, but rather liability extending only to the assets of the estate he is administering. Trustee O'Neill's dire predictions about the potential personal consequences to a trustee when abandonment is disallowed are thus unfounded.

Similarly unfounded are petitioners' assertions that the State or federal government should finance all of the

remedial work needed at the Edgewater site despite the availability of assets in the Quanta estate that could be used, at the very least, to provide some stabilization and cleanup activity. First, both New Jersey and federal law reflect a legislative policy favoring responsible party cleanups whenever private funds are available. *N.J.S.A.* 58:10-23.11 *et seq.*, (Spill Act); 42 *U.S.C.* § 9601 *et seq.*, (CERCLA). *See also* H. Rep. No. 1016, Pt.I, 96th Cong., 2d Sess. (1980), reprinted in 1980 U.S. Code Cong. & Ad. News 6119, 6120, where it was noted that one objective of the liability provisions in CERCLA was "to induce such [liable] persons voluntarily to pursue appropriate environmental response actions with respect to inactive hazardous waste sites." The Spill Act goes as far as to make State expenditures a lien against the property of the discharger, with priority in some circumstances over other liens, in order to enhance the State's access to private funds for cleanup work. *N.J.S.A.* 58:10-23.11f(f); *Kessler v. Tarrats,* 194 *N.J.Super.* 136, 146, 476 *A.*2d 326, 331 (App. Div. 1984). This emphasis on private funding of cleanups whenever possible stems from a recognition that government funding is simply not sufficient to cover the vast number of cleanups that must be undertaken to protect the public health and the environment. In enacting CERCLA, Congress directed that federally funded cleanups proceed according to a priority list (42 *U.S.C.* §9605), and acknowledged that the moneys it was making available would allow for cleanups at only the most hazardous sites. *See* S.Rep. No. 848, 96th Cong., 2d Sess. at 17. Given these circumstances, the government's access to private funds for cleanup purposes must be assured whenever possible, including when private funds are available from an estate in

liquidation. Here, the trustee's action deprived New Jersey of assets in the Quanta estate, maintained a hazardous condition at the Edgewater site, and delayed cleanup activities for several years. Endorsing the State's position in this case would ensure that such an unfortunate scenario is never repeated.

In conclusion, it is beyond doubt that the hazardous conditions at the Quanta site and the trustee's failure to take any action whatsoever to remedy those conditions constituted a nuisance and violated many State and federal laws enacted to protect the public. Abandonment under these circumstances would be at least as ill-advised as the abandonment of the barges in *Ottenheimer v. Whitaker, supra,* 198 *F.*2d at 290, or the abandonment of the faulty pipes, vents, and manholes in *Lewis Jones, supra,* 1 Bankr. Ct. Sec. at 280. Indeed, abandonment here would in all likelihood be much more dangerous. The court below thus correctly invoked the public safety exception to the abandonment power implicit in 11 *U.S.C.* §554 in finding abandonment of the contaminated waste oil improper.

POINT II

THE ENFORCEMENT OF STATE REGULATORY LAWS DESIGNED TO PROTECT THE PUBLIC AGAINST A CORPORATION IN LIQUIDATION DOES NOT FRUSTRATE FEDERAL BANKRUPTCY OBJECTIVES AND THUS COMPLIES WITH THE SUPREMACY CLAUSE.

Petitioners argue that the enforcement of State police power laws to limit abandonment under 11 *U.S.C.* § 554 frustrates the objectives of federal bankruptcy law and is consequently preempted by the Supremacy Clause

of the Constitution, Art. VI, cl. 2. Since Congress incorporated judge-made law into its codification of the abandonment power—including the judicially-formulated public safety exception—the enforcement of State laws to protect the public is completely consistent with federal bankruptcy law. *See* Point I, *supra*. No question of preemption thus arises in this case. Even if one were to view § 554 independently of pre-Code abandonment law, however, the enforcement of State public health and safety laws should nonetheless be upheld against a Supremacy Clause challenge because Congress, in adopting bankruptcy legislation, fully intended neither to abrogate the police powers of the states nor to provide a haven for polluters.

As the court below noted, preemption analysis starts with the basic assumption that Congress did not intend to displace State law, citing *Maryland v. Louisiana,* 452 *U.S.* 725, 746 (1981). State laws are thus presumed valid under the Supremacy Clause, and preemption is disfavored, to be found only in the clearest cases of conflict. *Ibid.; Chicago and North Western Transportation Co. v. Kalo Brick & Tile Co.,* 450 *U.S.* 311, 317 (1981). This presumption of validity requires that exhaustive attempts to harmonize state and federal laws be made; only where that search for accommodation fails will the statute be stricken. *Florida Lime and Avocado Growers v. Paul,* 373 *U.S.* 132, 141-143 (1963).

Since this case involves the police powers of the states, it is also important to note that these powers are among the "least limitable" of all governmental powers. *Queenside Hills Realty Co. v. Saxl,* 328 *U.S.* 80, 82 (1946).

The authority of states to regulate businesses and property within their jurisdictions to prevent and abate health hazards and public nuisances has long been recognized as a primary function of the police power. *Northwestern Fertilizing Co. v. Hyde Park,* 97 *U.S.* 659 (1878). And where such historic police powers of the states are challenged under the Supremacy Clause, they must not be superseded "unless that was the clear and manifest purpose of Congress." *Rice v. Santa Fe Elevator Corp.,* 331 *U.S.* 218, 230 (1947). Preemption analysis thus requires careful scrutiny of each of the laws in question to determine whether the exercise of state powers would constitute an obstacle to the effectuation of federal objectives. *Perez v. Campbell,* 402 *U.S.* 637, 649 (1971).

In enacting 11 *U.S.C.* § 554 and permitting a trustee in bankruptcy to abandon property that was worthless or burdensome, Congress sought to facilitate the reduction of the debtor's property to money for distribution to creditors. 4 *Collier on Bankruptcy* § 554.01 (15th ed. 1985). In liquidation proceedings, it is the responsibility of the trustee to collect the debtor's assets, reduce them to money, and then distribute the property of the estate. 11 *U.S.C.* § 704. The ability to abandon burdensome property consequently assists the trustee in the administration of the estate and serves the interests of creditors by speeding settlement of their claims.

The purpose of the Spill Compensation and Control Act, *N.J.S.A.* 58:10-23.11a *et seq.*, is to protect the public and the environment by prohibiting the discharge of hazardous substances. Where discharges have occurred, the Spill Act provides for liability against responsible parties

for cleanup costs and other damages associated with the discharge. *N.J.S.A.* 58:10-23.11f; *N.J.S.A.* 58:10-23.11g. The purpose of the Solid Waste Management Act, *N.J.S.A.* 13:1E-1 *et seq.,* is to regulate the storage, treatment, and disposal of waste to ensure that these activities are performed properly in furtherance of the public interest.

To ascertain congressional intent as to the interaction of § 554 and public safety regulations, it is necessary to look beyond the abandonment provision to the bankruptcy laws as a whole. For, "[w]hen 'interpreting a statute, the court will not look merely to a particular clause in which general words may be used, but will take in connection with it the whole statute . . . and the objects and policy of the law, as indicated by its various provisions, and give to it such a construction as will carry into execution the will of the Legislature . . . .' " *Kokoszka v. Belford,* 417 *U.S.* 642, 650 (1974), quoting *Brown v. Duchesne,* 60 *U.S.* (19 *How.*) 183 (1857). In looking beyond § 554, it is evident that Congress did not intend the bankruptcy laws to abrogate the enforcement of police power regulations by the states.

A primary example of this policy is found in the automatic stay provision of the Bankruptcy Code. There Congress specifically provided that the filing of a bankruptcy petition would not operate as a stay "of the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power." 11 *U.S.C.* § 362(b) (4). *See also* 11 *U.S.C.* § 362(b) (5) which exempts from the automatic stay the enforcement of all pre-petition judgments, except for money judgments, that were obtained in an action by a governmental unit to enforce its police or regulatory powers; *Ohio v. Kovacs, supra,* 105 *S.Ct.* at 711 n. 11; *Penn Terra Ltd. v. Dept. of Env. Resources,* 733 *F.*2d 267, 272-273 (3d Cir. 1984) (upholding enforcement of State anti-pollution laws through execution of pre-petition judgment as consistent with exception to automatic stay under 11 *U.S.C.* § 362(b) (5), despite the fact that compliance with the judgment by the company would deplete assets otherwise available to creditors). Congress crafted these exceptions to the automatic stay so that they would apply "where a governmental unit is suing a debtor to prevent or stop violation of . . . environmental protection . . . laws, or attempting to fix damages for violation of such a law." S. Rep. No. 989, 95th Cong., 2d Sess. 52, reprinted in 1978 U.S. Code Cong. & Admin. News 5838. The need for these exceptions arose because under prior law the bankruptcy stay had been abused to restrict enforcement of vital government regulations. These abuses were typified by the order of a bankruptcy court preventing a state from closing a debtor's plant that was polluting a river in violation of the state's environmental protection laws. H. Rep. No. 595, 95th Cong., 1st Sess. 174-175 (1977), reprinted in 1978 U.S. Code Cong. & Admin. News 6135. By adopting 11 *U.S.C.* § 362(b) (4) and (5), Congress demonstrated unequivocally that bankruptcy laws should not be permitted to override vital state police power regulations. This congressional action establishes that when public safety is at issue, bankruptcy policy must yield to higher priorities. *Penn Terra Ltd. v. Dept. of Env. Resources, supra,* 733 *F.*2d at 278; *Matter of Canarico Quarries, Inc.,* 466 *F.Supp.* 1333, 1337 (D.P.R. 1979) (court refused to stay environmental agency from executing an agreement

in which the debtor was required to install air pollution control equipment despite the significant cost of these measures).

A similar conclusion is drawn from reference to 28 *U.S.C.* § 959(b) which explicitly requires the trustee in his management and control of the property of the estate to obey all valid state laws. 28 *U.S.C.* § 959(b) provides, in relevant part:

> . . . a trustee . . . shall manage and operate the property in his possession . . . according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

This statute demonstrates that Congress did not intend to permit trustees to abandon worthless property when such abandonment would violate state law. In this instance, for example, because the abandonment of the Edgewater facility with its hundreds of thousands of gallons of PCB-contaminated materials would violate New Jersey law, abandonment would directly conflict with the requirements of § 959(b) and would be prohibited.

Petitioners dispute this reliance on 28 *U.S.C.* 959(b), however, alleging that this statutory provision applies only in the Chapter 11 reorganization context and does not cover a business in liquidation. The court below questioned this unduly narrow interpretation, and declined to endorse it. This Court should follow that lead by holding that § 959(b) applies to liquidations as well as to reorganizations.

First, Congress used the word "manage" in § 959(b). This term encompasses both administering an estate and

conducting a business. *See* Black's Law Dictionary 865 (rev. 5th ed. 1979), defining "manage" as "to control and direct, to administer, to take charge of. To conduct; to carry on the concerns of a business or establishment." *Accord, Webster's Third New International Dictionary* 1372 (1976), defining "manage" as "to control and direct" or "administer." There consequently is no basis in the statutory language for limiting § 959(b) to the reorganization context.

Moreover, in 28 *U.S.C.* § 959(a), Congress provided that, "Trustees, receivers or managers of any property, including debtors in possession, may be sued, without leave of the court appointing them, with respect to any of their acts or transactions ***in carrying on business*** connected with such property." (emphasis added). This provision has been interpreted to refer to the operation of a business under a Chapter 11 reorganization plan. *Matter of Campbell,* 13 *Bankr.* 974, 976 (D. Idaho, 1981). Should Congress have wanted to limit § 959(b) in similar fashion, it would have repeated the same statutory language. Instead, Congress broadened the effect of the obligation to comply with State law beyond the context of "carrying on business" to reach all activities involved in managing a property in bankruptcy, including a business in liquidation, except for those activities expressly excluded from the reach of § 959(b), and not relevant here.

Perhaps even more telling in regard to the reach of § 959(b) is that Congress made the *possession* of property the pivotal concept for coverage, requiring the trustee to manage property in his possession in the same manner—and subject to the same laws—that the owner would be bound to follow if the property were in his possession.

The concept of possession applies in liquidation as well as in reorganization. In cases under all chapters, the trustee is the representative of the estate. 11 *U.S.C.* § 323(a). In this capacity, the trustee acquires control over and possession of the property of the estate, and may use, sell, or lease the property after notice and hearing. 11 *U.S.C.* § 363(b)(1). Since the trustee in liquidation cases certainly "manages" the property of the estate in his "possession," as the trustee here managed the Quanta estate in the process of selling and abandoning the debtor's property, such administrative actions must comply with "the valid laws of the State in which such property is situated." 28 *U.S.C.* § 959(b). Petitioners have cited no case law on point to the contrary.* Indeed, in *In re Chicago Rapid Transit Co., supra,* 129 *F.*2d at 5-9, the court relied upon the statutory predecessor of § 959(b) in directing the trustee to comply with state law in his attempt to liquidate a part of the debtor's business. The state law in issue there prohibited the trustee from discontinuing service on a branch railway line until receiving permission from the Illinois Commerce Commission. Rather than creating obligations for the corporation in the conduct of its business, this type of regulation concerns the fundamental managerial perrogative, *i.e.,* whether to conduct business at all. Accordingly, the *Chicago Rapid*

* Although petitioners cite *State of Missouri v. U.S. Bankruptcy Court,* 647 *F.*2d 768, 778 (8th Cir. 1981), *cert. den.* 454 *U.S.* 1162 (1982), to support their argument that § 959(b) applies only in the reorganization context, the Court of Appeals there expressly refused to decide this issue, and did not discuss it thoroughly. Moreover, the context of the *Missouri* case involved a financial responsibility law that went more to the pecuniary interests of the state than to its regulatory interests and thus is distinguishable from the instant matter.

Transit case presents an instance in which a trustee was required to comply with valid State laws in his management of the estate. This precedent lends support to an interpretation of § 959(b) that reaches the administration context, including the administration of an estate in liquidation.* *See also Ohio v. Kovacs, supra,* 105 *S.Ct.* at 711-712, where the Court noted that it did not question the responsibility of anyone in possession of a hazardous waste site—including a trustee in bankruptcy in a liquidation proceeding—to comply with state environmental laws.

Courts regularly apply 28 *U.S.C.* §959(b) to require bankruptcy trustees to comply with State law. In *Gillis v. California,* 293 *U.S.* 62 (1934), a receiver of a corporation in reorganization asked the Court to sanction noncompliance with a state licensing law, contending that the exemption was necessary to keep the business in operation. Citing the statutory predecessor to § 959(b), the Court denied the request and upheld the applicability of the state licensing requirements despite the consequences

* Although petitioners cite 2 *Moore's Federal Practice* (2d ed. 1982) § 66.04[4] for the proposition that 28 *U.S.C.* § 959(b) requires a trustee to adhere to state law only when operating a business under a Chapter 11 reorganization plan, this reliance is misplaced. In context, the excerpt from *Moore's* establishes merely that § 959(b) does not compel the trustee to obey state laws governing preferences in the distribution of funds. The correctness of this interpretation of *Moore's* is established by an examination of the entire paragraph and by the case cited there, *First Nat. Bank v. Ewing,* 103 *F.*2d 168, 193-195 (5th Cir. 1900), *cert. den.* 179 *U.S.* 686 (1900) (holding that the statutory predecessor of § 959(b) did not require a trustee to obey state laws defining the priority of creditors). The treatise does not address the issue of import here: whether § 959(b) compels a trustee in possession of a debtor's property to adhere to State law in his management of that property in the course of a liquidation proceeding.

to the business. *See also Matter of Canarico Quarries, Inc., supra,* 466 *F.Supp.* at 1339 (holding that § 959(b) requires compliance with environmental regulations despite the cost); *Colonial Tavern, Inc. v. Byrne,* 420 *F.Supp.* 44 (D. Mass. 1976) (suspension of liquor license upheld for repeated violations of midnight closing hour regulations); *Commonwealth v. Peggs Run Coal Co.,* 423 *A.*2d 765 (Pa. Commw. Ct. 1980) (allowing the closing of a coal production facility which was violating local environmental resource laws). Although these cases arose in the reorganization context, they support applying § 959(b) in liquidation proceedings as well. For the courts in those reorganization cases were willing to apply state laws even though that action would frustrate both the interests of creditors who wanted to preserve the estate to maximize their own recoveries, and the debtor's interest in rehabilitating the business. Since only the former concern of the creditors would be thwarted in the liquidation context, there is no reason not to apply § 959(b) to liquidations where—if anything—the application of state law would have less of an impact on bankruptcy proceedings than in the reorganization context.

Section 959(b) thus reflects a definite legislative intent to require compliance with state police power regulations. When viewed together with the exception to the automatic stay for governmental enforcement actions of a public safety nature, 11 *U.S.C.* § 362(b) (4), a clear congressional policy favoring the maintenance of state regulatory activities in the bankruptcy context emerges. Interpreting 11 *U.S.C.* § 554 to allow for an exception to the abandonment power where the public would be at risk and state law violated consequently complies with the objectives of Congress and the dictates of the Supremacy Clause.

Although the court below limited its discussion of public safety regulations to those contained in state law, it is beyond question that federal environmental laws also apply to this matter and were violated by the improper storage and continuing leaks of contaminated oil at the Quanta site. Such federal violations have in fact been confirmed by the recent removal action taken by the United States Environmental Protection Agency at the Edgewater facility under CERCLA, 42 *U.S.C.* § 9601 *et seq. See also* TSCA, 15 *U.S.C.* § 2601 *et seq.* Viewing the issue here solely as one of preemption is thus shortsighted. For the interaction of the bankruptcy and environmental laws also raises questions concerning the relationship between federal enactments with decidedly different purposes. In such a situation, courts are required to regard each statute as effective whenever—as is the case here—they are capable of coexistence and there is no clearly expressed congressional intent to the contrary. *See Ruckelshaus v. Monsanto Co., supra,* 104 *S.Ct.* at 2881; *Morton v. Mancari,* 417 *U.S.* 535, 551 (1974). Consideration of this factor bolsters NJDEP's position that state as well as federal environmental laws should be given full effect in the bankruptcy context.

Despite the claims of petitioners, upholding the public safety exception to the abandonment power and allowing enforcement of either or both state and federal environmental laws does not run counter to this Court's recent decision in *Ohio v. Kovacs, supra,* 105 *S.Ct.* at 705. At issue in *Kovacs* was the extremely narrow question of whether a pre-bankruptcy obligation of an individual (as

opposed to a corporate) debtor to comply with a state court injunction requiring him to clean up a hazardous waste site was a "debt" that was "dischargeable" under the Bankruptcy Code. *See* 11 *U.S.C.* § 101(4)(B); 11 *U.S.C.* § 727(b). In *Kovacs,* the debtor had been removed from control of the waste site prior to a bankruptcy filing, and had been replaced by a receiver who was directed to comply with the injunction that the debtor had failed to implement. Subsequently, after the bankruptcy filing, Ohio sought to obtain part of the debtor's post-bankruptcy income for use in completing the cleanup. Since the receivership had effectively prevented the debtor from carrying out the cleanup himself, the Court held that the cleanup obligation had been converted into an obligation to pay money—an obligation that was dischargeable through bankruptcy. 105 *S.Ct.* at 710-711.

In reaching this conclusion, the Court in *Kovacs* distinguished *Penn Terra, Ltd. v. Dept. of Env. Resources, supra,* 733 *F.*2d at 267, which had found that a state action seeking an injunction against a bankrupt and requiring compliance with environmental laws was not a suit to enforce a money judgment, but rather an action to enforce the police powers of the State and thus was exempt from the automatic stay. 105 *S.Ct.* at 711 n. 11. Similarly, NJDEP's administrative order directing Quanta to remedy the hazardous discharges at the site and to remove the contaminated oil, and the State's opposition to abandonment as constituting a violation of the environmental laws, represents State action taken in a police power, and not a pecuniary capacity. *Kovacs* is distinguishable from the instant case on this ground. Although a footnote in *Kovacs* referred to a hypothetical situation where a trus-

tee would abandon property under 11 *U.S.C.* § 554 to the debtor if the polluted property were worth less than the cost of cleanup, 105 *S.Ct.* at 711 n. 12, this suggestion did not absolve the trustee or the debtor from complying with State environmental laws while the property was in their possession. In fact, the Court specifically asserted that, "we do not question that anyone in possession of the site—whether it is Kovacs or another in the event the receivership is liquidated and the trustee abandons the property, or a vendee from the receiver or the bankruptcy trustee—must comply with the environmental laws of the State of Ohio." 105 *S.Ct.* at 711-712. Nor did the Court address the public safety exception to the abandonment power which is at the heart of this case. The question here—upon which *Kovacs* is silent—is whether abandonment to an assetless corporate shell is appropriate in the face of an ongoing discharge of hazardous substances where the trustee has assets available to finance some remedial or stabilization activity, has refused to use those assets to fund any cleanup action whatsoever, and where abandonment would be tantamount to disposal of the waste oil and rendering the site a ward of the government. Under these circumstances, as demonstrated above, abandonment would be both inappropriate and dangerous. *Kovacs* does not hold to the contrary.

The distinction made in *Kovacs* and in *Penn Terra, supra,* 733 *F.*2d at 267, between state actions of a police power and a pecuniary nature is a critical one, however. It is a distinction codified in the automatic stay provision, 11 *U.S.C.* §362, and a distinction that arises in non-bankruptcy contexts such as interstate commerce. *See Reeves, Inc. v. Stake,* 447 *U.S.* 429, 439 (1980) (distinguishing be-

tween states as market participants and as market regulators for purposes of the Commerce Clause). The automatic stay provision is particularly illuminating in this regard because it clearly reflects a distinction made by Congress in the bankruptcy context between government as regulator and government as creditor. *See In re Thomassen*, 15 *Bankr.* 907, 909 (Bankr. 9th Cir. 1981); H. Rep. No. 95-595, 95th Cong., 1st Sess. at 343, *reprinted in* 1978 *U.S. Code Cong. & Admin. News* at 6299. Petitioners' failure to see this distinction, and their mischaracterization of NJDEP as a creditor, have led them to assert that the Supremacy Clause requires abandonment in this case because, absent that, states would be able to devise a preference over other creditors that would frustrate the priority distribution system established in the Bankruptcy Code. Analysis of this contention demonstrates that petitioners have manufactured a conflict between the Code and police power regulations where no real conflict exists.

In seeking to enforce compliance by the trustee with applicable environmental protection laws, the State is plainly acting in its regulatory capacity. The State's enforcement of its environmental regulations seeks compliance by the trustee with the law in the same manner as any similarly situated party; it does not constitute the act of a creditor trying to devise a preference over other creditors. *See In re Dolly Madison Industries, Inc.*, 504 *F.*2d 499, 503 (3d Cir. 1974) ("The mere fact that the debtor's property may be affected by state law does not constitute a 'claim' against that 'property' . . . ").

The flaw in petitioners' characterization of the environmental enforcement actions of the State as the acts of a

creditor is amply demonstrated by extending petitioners' interpretation to other sections of the Code. For example, if the State's enforcement actions constitute acts of a creditor, then any expenditures to ensure compliance with pollution laws made by a debtor within 90 days before filing of its bankruptcy petition would be subject to avoidance by the trustee as a preferential transfer. 11 *U.S.C.* §547(b). In that event, the State would be required to reimburse the estate for the cost of the environmental protection measures undertaken by the debtor immediately before its bankruptcy filing. The absurdity of this statutory interpretation demonstrates the fundamental error in petitioners' characterization of the State as a creditor in this instance. Because the State's efforts to ensure compliance with the environmental laws are actions in its regulatory capacity, its actions in no way frustrate the distributional priorities set forth in the Code.

Finally, petitioner Midlantic National Bank has asserted that the provisions of the Environmental Cleanup Responsibility Act ("ECRA"), *N.J.S.A.* 13:1K-6 *et seq.*, enacted by the New Jersey Legislature on September 2, 1983, conflict with federal bankruptcy law and must be invalidated under the Supremacy Clause. The short answer to this contention is that the statute does not apply here because ECRA did not exist in May 1983 when the Bankruptcy Court approved abandonment of the contaminated waste oil, and hence was not addressed below. Midlantic's preemption challenge to ECRA thus has no place in this lawsuit and should be dismissed by the Court. Were the issue to be entertained, however, the preemption challenge should be rejected because ECRA is fundamentally a state law that defines property rights and "Congress

has generally left the determination of property rights in the assets of a bankrupt estate to state law." *Butner v. United States,* 440 *U.S.* 48, 54 (1979), cited in *Ohio v. Kovacs, supra,* 105 *S.Ct.* at 712 (O'Connor, J. concurring). *See Johnson v. First Nat'l Bank of Montevideo,* 719 *F.*2d 270, 273 (8th Cir. 1983) (state property law is not preempted and governs in bankruptcy unless state law and Bankruptcy Code are in actual conflict). In fact, the legislative requirements imposed by ECRA represent just the kind of statutory solution proposed by Justice O'Connor to protect the state's right to the assets of a bankrupt for cleanup purposes. *Ibid.*

Neither ECRA nor the enforcement of other state environmental laws to prevent abandonment and protect the public safety stand as an obstacle to the achievement of congressional bankruptcy objectives. This Court must consequently reject petitioners' unfounded preemption challenge and affirm the decision below.

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POINT III

THE ENFORCEMENT OF THE PUBLIC SAFETY EXCEPTION TO THE ABANDONMENT POWER POSSESSED BY A TRUSTEE IN BANKRUPTCY DOES NOT "TAKE" THE PROPERTY OF CREDITORS AND THUS IS CONSISTENT WITH THE TAKING CLAUSE OF THE CONSTITUTION.

Although the court below held that abandonment would not be appropriate in this case because of the public health risk associated with such an action, it expressly refused to reach the issue of how the remaining assets in the estate should be distributed. 739 *F.*2d at 923. In regard to the New Jersey case, the court stated that, "The issue is not who should pay to clean up the estate's property; it is whether the Trustee's interest in preserving the estate should prevail over the public's interest in containing the hazards produced by toxic wastes in the possession of the estate." 739 *F.*2d at 929. In light of this holding, the court remanded the cases to the Bankruptcy Court for further proceedings, including the development of a factual record and a determination of the priority, if any, of the rights of the states to the remaining assets. *Ibid.;* 739 *F.*2d at 923. The record before this Court thus fails to reveal the impact on Quanta's creditors of the decision to prevent abandonment of the contaminated oil. The assertion made by petitioners that interpreting 11 *U.S.C.* §554 to prevent abandonment here "takes" the property of creditors without just compensation is consequently premature at best and should not be addressed by this Court. Even if one assumes that most, or all, of the assets in the Quanta estate would be used—absent abandonment—to stabilize the leaky tanks and otherwise perform remedial activities at the Edgewater site, however, such use of the assets would not represent a "taking" in the constitutional sense.

First, petitioners apparently concede that the application of environmental laws to a corporation not seeking the protection of the Bankruptcy Code presents no constitutional infirmity even though compliance with these regulations can require the expenditure of substantial sums of money. Indeed, given the paramount public purpose served

by protecting the public and the environment from exposure to toxic contaminants, it cannot be doubted that these laws are proper governmental enactments that do not constitute an illegal taking of private property. *See generally Ruckelshaus v. Monsanto Co., supra,* 104 *S.Ct.* at 2875-2876, where the Court noted in regard to pesticide regulations that, "such restrictions are the burdens we all must bear in exchange for 'the advantage of living and doing business in a civilized community.'" (citations omitted). Although the Third Circuit did not decide the "taking" issue and remanded both the New York and New Jersey cases to the Bankruptcy Court for the development of a factual record regarding a distribution of assets, the court did cite numerous precedents rejecting taking challenges when the state had exercised its regulatory powers to promote the public good. 739 *F.*2d at 922 n. 11. Of particular note among the cases cited are *Goldblatt v. Town of Hempstead,* 369 *U.S.* 590 (1962) (upholding a local ordinance prohibiting excavation below the water table as a valid exercise of the police power despite the fact that the ordinance prevented an excavating company from carrying on its business as intended), and *Miller v. Schoene,* 276 *U.S.* 272 (1928) (upholding against a "taking" challege the destruction of red cedar trees to prevent the spread of rust disease harmful to apple orchards in the vicinity).

In spite of the unquestionable constitutionality of laws governing hazardous waste disposal, petitioners argue that enforcement of environmental laws of general applicability in the context of a corporation in bankruptcy liquidation will constitute a taking of the property in-

terests of secured creditors.* This contention is grounded on the assumption that because the cost of stabilizing and properly disposing of the PCB-contaminated oil will exceed the value of the collateral to which their secured interest attaches, application of environmental regulations will *a fortiori* constitute a governmental taking of their security interest. This constricted analysis fails to assess accurately the nature of the governmental and private interests at issue in this matter, and must be rejected.

State and federal laws governing the storage, disposal, and discharge of PCB-contaminated waste oil are of universal application and applied to Quanta throughout its operating life. During that period, Quanta at all times was legally responsible for rejecting PCB's and, failing that, for ensuring the proper containment and disposal of the contaminated oil. *See generally* the Solid Waste Management Act, *N.J.S.A.* 13:1E-1 *et seq.* (enacted in 1970), and the regulations adopted thereunder, *N.J.A.C.* 7:26-1 *et seq.;* the Spill Compensation and Control Act, *N.J.S.A.* 58:10-23.11a *et seq.* (enacted in 1977); TSCA, 15 *U.S.C.* § 2601 *et seq.* (enacted in 1976); and CERCLA, 42 *U.S.C.* § 9601 *et seq.* (enacted in 1980). It is difficult to understand how these valid police power regulations are transformed into unconstitutional takings simply be-

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* Although the trustee of the Quanta estate implies that the property rights of unsecured creditors will be taken unless abandonment is permitted in this matter, see Brief for Petitioner Thomas J. O'Neill, Trustee, at 12, it is highly unlikely that unsecured creditors will receive any distribution from the Quanta estate, regardless of the resolution of the abandonment question and related legal issues. As a result, the discussion in this brief will be confined to an analysis of the claims of secured creditors of the estate.

cause of the insolvency of a corporation which is subject to the laws.

Despite the contentions of Midlantic, the enforcement of these toxic waste laws in bankrutpcy is neither unfair nor unconstitutional. For when Midlantic made its loan to Quanta, it did so against a backdrop of environmental laws that placed Quanta in a highly regulated business. *See, e.g., N.J.S.A.* 13:1E-1 *et seq.; N.J.S.A.* 58:10-23.11a *et seq.;* 15 *U.S.C.* § 2601 *et seq.;* 42 *U.S.C.* § 9601 *et seq.* Midlantic thus knew—or should have known—that Quanta had a legal obligation to operate its potentially hazardous business in accord with applicable police power regulations enacted to protect the public. These legal responsibilities and the concomitant financial obligations associated with compliance significantly increased the risk of Quanta's insolvency and of the erosion or destruction of the collateral to which Midlantic's security interest attached. Had Quanta complied with the environmental laws to the fullest of its ability prior to the filing of its bankruptcy petition, the collateral to which Midlantic asserts a claim would have been exhausted and never become part of the estate.

The Bankruptcy Code, by not permitting abandonment in these circumstances and by requiring compliance with the environmental laws, recognizes the extremely risky position in which the bank had placed itself and seeks to ensure that the bankruptcy process does not improve this position. In making a loan to Quanta, Midlantic must have assumed that the corporation was sufficiently viable to pay off the loan while complying with the environmental laws. By arguing now that the estate

need not comply with these same regulations, Midlantic is trying to alter the risk that it voluntarily accepted in the loan transaction, and is seeking to transfer that risk to the public. As this Court has previously recognized, "it is a fundamental aspect of our free enterprise economy that private persons assume the risks attached to their investments," *New Haven Inclusion Cases,* 399 *U.S.* 392, 492 (1970), quoting *Penn-Central Merger Cases,* 389 *U.S.* 486, 510 (1968). Far from constituting a "taking," therefore, interpreting 11 *U.S.C.* § 554 to prevent abandonment in this case would simply prevent Midlantic from transferring to the public a financial risk it knowingly assumed.

A key element in this analysis is that the value of Midlantic's security interest was diminished by the illegal actions of Quanta in accepting PCB wastes at the Edgewater facility, and not by governmental regulation of the contaminated property. A New Jersey court has recognized this proposition in a context similar to the one here. In upholding against a taking challenge the priority lien provision of the Spill Compensation and Control Act, *N.J.S.A.* 58:10-23.11f(f), the court in *Kessler v. Tarrats, supra,* 194 *N.J. Super.* at 136, 476 *A.*2d at 326, asserted that:

> The State's involvement with this property began because of the contamination of the premises with hazardous substances. We cannot in this discussion overlook the negative impact on property values by the presence of toxic wastes; the unquestioned authority of the State to require abatement of a health nuisance, and the ability of government to close down a property or facility which creates a public health menace. See *Paterson v. Fargo Realty, Inc.,* 174

> *N.J. Super.* 178, 183 (Cty. D.Ct. 1980). The illegal dischargers are responsible for the physical damage to the property and any corresponding diminution in market value thereof. Whatever diminution in value may have occurred to affect plaintiff's security interest was as the result of the acts of polluting the property. Therefore, whatever property, if any, was "taken" was taken by the dischargers of the hazardous substances and not by the State. [194 *N.J. Super.* at 146-147; 476 *A.*2d at 332].

Application of the *Kessler* analysis to the facts of the instant case demonstrates that no governmental taking of property has occurred, for the Constitution does not require the states to indemnify creditors for bad business decisions.

When Quanta violated the environmental laws, it also betrayed the trust of Midlantic. Although Midlantic wants to protect its security interest despite this betrayal and the consequences to the public of Quanta's illegal action, the rights of creditors are not absolute. Indeed, the public interest takes precedence and "is not merely a pawn to be sacrificed for the strategic purpose or protection of a class of security holders." *Penn-Central Merger Cases, supra,* 389 *U.S.* at 510-511. Such principles are even more pertinent here than in the railroad context since the public safety, and not just public convenience, is at stake. *See also Home Building & Loan Ass'n v. Blaisdell,* 290 *U.S.* 398 (1934), where the Court upheld a state law that altered pre-existing contractual agreements in order to assist homeowners caught in the economic emergency conditions caused by the Depression. The Court concluded there that states retain the power to protect the public—including the power to protect the public from the maintenance of nuisances—despite the impact that the exercise of such police powers would have on existing contracts. 290 *U.S.* at 436. Similar reasoning applies here in the "taking" context and supports the rejection of the constitutional challenge raised by petitioners.

Nothing in *United States v. Security Industrial Bank,* 459 *U.S.* 70 (1982), requires a contrary result. In that case, a "taking" challenge was brought against 11 *U.S.C.* § 522(f)(2) which permitted individual debtors in bankruptcy proceedings to avoid liens on certain property. The Court there refused to apply the statute retroactively to avoid what it found to be "substantial enough constitutional doubts to warrant" prospective operation only. The constitutional doubts in *Security Industrial Bank* arose because the bankruptcy law itself authorized the abrogation of otherwise valid and valuable security interests. No question of public safety was involved. Here, by contrast, neither the operation of the environmental laws, nor the application of the public safety exception to the abandonment power, abrogate security interests. Rather, secured creditors suffered losses at the hands of the debtor whose illegal actions diminished or destroyed the value of the security interests. All the State tried to do in preventing abandonment was to ensure that its undoubtedly constitutional regulatory laws were enforced to the greatest extent possible to protect the public. Since these facts support neither a taking violation nor create "substantial doubts" suggesting a possible taking by operation of federal or state law, *Security Industrial Bank* is inapposite.

Should this Court decide to reach the "taking" issue, therefore, it should reject petitioners' challenge and uphold the constitutionality of the public safety exception to the abandonment power.

CONCLUSION

For all of the foregoing reasons, NJDEP urges this Court to affirm the decision of the United States Court of Appeals for the Third Circuit holding that abandonment of PCB-contaminated oil by the trustee in bankruptcy was not appropriate under 11 *U.S.C.* § 554 because of the danger to the public safety associated with such abandonment.

Respectfully submitted,

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DATED: June 6, 1985

(10) (11)

Nos. 84-801 and 84-805

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,

Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK and THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,

Respondents.

MIDLANTIC NATIONAL BANK,

Petitioner,

v.

THE NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,

Respondent.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF OF RESPONDENTS STATE OF NEW YORK AND CITY OF NEW YORK

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Questions Presented

1. Does section 554(a) of the Bankruptcy Code authorize a trustee in bankruptcy to abandon a toxic waste facility which constitutes a present hazard to public health, safety and the environment, in violation of federal, state and local laws?

2. Would an order of the bankruptcy court limiting the trustee's authority to abandon the facility under these circumstances constitute an unlawful taking of the secured creditors' interests (assuming that this issue is ripe for decision)?

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TABLE OF AUTHORITIES

Statement of the Case

This case involves a bankruptcy trustee's negligent post-petition management of a hazardous waste facility in the heart of the nation's largest city. The bankruptcy trustee managing this property took virtually no steps during his administration of the estate to protect the public from leaking chemicals or possible fires; then, after nearly eight months of neglect, he simply decided to abandon the property. New York opposed this effort.

This case also involves the harmonization of important federal and state policies: on the one hand, to protect the health and safety of the American public from the toxic effect of dangerous chemicals by preventing their uncontrolled discharge into the environment, and on the other, by means of federal bankruptcy policy, to provide a fair distribution of a debtor's assets among creditors. The court below carefully accommodated these policies in order to protect the public. This Court should reject the petitioner's attempt to upset that careful balance.

****

Quanta Resources Corporation ("Quanta" or the "debtor") was in the business of collecting, transporting, processing and storing waste oils. *In re Quanta Resources Corp.*, 739 F.2d 912, 913 (3d Cir. 1984) ("*Quanta*") (App. A, 1a, 3a).[1] Quanta owned and operated facilities in Edgewater, New Jersey and in Long Island City in New York City. *Id.* at 913 (App. A, 3a); *In re Quanta Resources Corp.*, 739 F.2d 927, 928 (3d Cir. 1984) (App. B, 37a).[2]

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[1] References to pages in the appendices to the Petition for a Writ of Certiorari are indicated as App. ____, ____. References to pages in the joint appendix in the court below are indicated as J.A. ____.

[2] Before their sale to Quanta, these facilities were operated by companies reportedly controlled by Russell W. Mahler, President of the former Hudson Oil Refining Company, who was convicted of illegal dumping of toxic wastes into abandoned mines in Pennsylvania and sentenced to serve one year in prison and pay a $750,000 fine. Chavez, *Toxic Waste Entrepreneur*, N.Y. Times, May 27, 1982, D 1 at col. 1; Blumenthal, *Accused Polluter Was Paid to Clean Up Sites*, N.Y. Times, May 7, 1982, B 20 at col. 1.

The Long Island City toxic waste facility is located at the geographic center of New York City, *Quanta*, 739 F.2d at 913 (App. A, 3a), and is approximately 450 feet from Newtown Creek, a tributary of the East River, a navigable waterway. More than 500,000 gallons of waste oil, sludge and hazardous waste were being stored on the property; more than 70,000 gallons of these were contaminated with polychlorinated biphenyls (PCB's), an extremely hazardous substance. *Id.* (App. A, 4a); Affidavit of James Reid (J.A. 17-18).

On October 6, 1981, Quanta filed a voluntary petition for reorganization under Chapter 11 of the Bankruptcy Code. *Id.* (App. A, 3a). After filing its petition for reorganization, Quanta continued in the operation of its business and in possession of its property as debtor-in-possession until November 12, 1981. *Id.* At that time, Quanta's reorganization case was converted to a Chapter 7 liquidation case and Thomas J. O'Neill, the petitioner ("trustee"), was appointed trustee. *Id.*

In June of 1982, after nearly eight months of neglect by the trustee, the facility was in a dangerous state of disrepair. *See* Affidavit of Richard Docyk (J.A. 11-13). Some of the storage tanks had holes in them, and some were leaking. *Id.* The system needed by the Fire Department to put out a fire was not in operation, and some of the equipment necessary to make the system effective was missing. Had a fire broken out, the burning waste oil would have generated smoke-laden PCB's, and possibly dioxin, threatening the lives of fire fighters and millions of New York City residents.[3] Affidavit of Dan Levy ("Levy Aff.") (J.A. 19-22).

[3] When PCB's are burned, heated to high temperatures, or exposed to sunlight, they are oxidized. Oxidized PCB's are much more toxic than the PCB's themselves. Oxidation products include the polychlorinated dibenzo-p-dioxins (commonly called dioxins) and polychlorinated dibenzofurans. There are many isotopes (varieties) of these compounds containing four chlorine atoms which are common oxidation products of PCB's. These tetrachlorodibenzo-p-dioxins (TCDD's) and tetrachlorodibenzofurans (TCBF's) include some of the most toxic compounds known. They are among the most potent carcinogens, teratogens, and liver toxins. Oral doses on the order of a few micrograms (a millionth of a gram) can be lethal. Levy Aff. (J.A. 21).

By notice dated May 25, 1982, the trustee proposed to abandon the Long Island City toxic waste facility on the grounds that the property is "burdensome to the estate, or . . . is of inconsequential value to the estate." 11 U.S.C. § 554(a) (1982). *See Quanta*, 739 F.2d at 913 (App. A, 4a). Assuredly, the facility was not being properly operated when the trustee took over possession and management. Nonetheless, as the City and the State of New York (hereinafter, when referred to collectively, "New York") argued, what the trustee proposed to do by abandonment, after having neglected the facility, created dangers to the public safety and the environment which would not have otherwise existed. Implicitly, by requesting approval to abandon, the trustee was requesting the court to approve the removal of guards and other supervisory personnel who had been placed there because of the dangerous condition of the facility. Previously, the trustee sought to sell components of the partially inoperable fire suppression system. (Notice of Proposed Private Sale by the Trustee, dated May 3, 1982). Additionally, the trustee sought to abandon the half-million gallons of flammable liquids contaminated with highly dangerous PCB's.

Permitting the trustee to abandon the Long Island City facility meant, in the view of New York officals, the further deterioration of the untended facility and the possibility of vandalism. This would substantially increase the possibility of fire or leakage and would seriously endanger the lives and property of New York residents. In addition to the public health problems that would be created, abandonment of the Long Island City facility by the trustee would effectively constitute final disposal of the PCB-contaminated oil and other hazardous wastes on the property because the debtor had been left without any assets.

New York consequently opposed abandonment of the toxic waste facility on the grounds that abandonment would endanger the safety of the public in violation of both federal and state law. *See* Objections to Proposed Abandonment, dated June 4, 1982 (J.A. 3). It asked the bankruptcy court instead to order that assets of the estate be used to bring the facility into compliance with

federal and state public safety and environmental laws.[4] *Id.* (J.A. 7). In the alternative, New York requested that any funds it expended to clean up the site constitute a first lien, taking priority over any other mortgages or liens on the property. *Id.*

On June 22, 1982, United States Bankruptcy Judge D. Joseph DeVito ruled that the trustee could abandon the Long Island City facility, stating:

> The City and State of New York are the proper parties to safeguard the health and safety of their citizens. The duty of the Trustee is to serve as representative of the estate, and the duty of this Court is to protect the assets of the estate in custodia legis.
>
> The City and State are in a better position in every respect than either the Trustee or debtor's creditors to do what needs to be done to protect the public against the dangers posed by the PCB-contaminated facility. But it is not the estate or debtor's creditors who should finance the requisite clean-up, given the decision of the Trustee to abandon the property.

Oral Decision (App. K, 73a). Judge DeVito also denied New York's motion to designate governmental funds spent on such a cleanup as constituting a first lien on the property.[5] *Id.* (App. K, 74a).

Notices of Appeal to the District Court of New Jersey were filed on July 16, 1982. Although Judge Lacey affirmed the order

[4] The trustee's allegation that there were no funds in the estate either to continue the security service at the Long Island City facility or otherwise to bring the site into compliance with government regulations, Brief for Petitioner Thomas J. O'Neill, Trustee ("T. Br.") at 5, is misleading. The estate in fact had significant assets which could have been converted into cash. For example, a portion of the waste oil inventory not contaminated with PCB's was sold, generating approximately $288,000.00. Brief of Petitioner, Midlantic National Bank ("Midlantic Br.") at 7.

[5] At the time of the petition to abandon, the Equitable Life Assurance Corporation and Portland Holding Corporation held mortgages on the property. Subsequently, both Equitable Life and Portland relinquished their mortgage interests. *Quanta*, 739 F.2d at 914 n.3 (App. A, 5a n.3). This issue of lien priority is therefore not before this Court.

of the bankruptcy court, he found that "the question is a close one." Memorandum Opinion, January 24, 1983, at 5 (App. G, 56a).[6]

New York filed a notice of appeal on February 17, 1983, and oral argument took place on October 24, 1983. On July 20, 1984, the court of appeals reversed the decisions of the bankruptcy and district courts. *Quanta*, 739 F.2d 912 (App. A, 1a). The court of appeals reasoned:

> If trustees in bankruptcy are to be permitted to dispose of hazardous wastes under the cloak of the abandonment power, compliance with environmental protection laws will be transformed into governmental cleanup by default. It cannot be said that the bankruptcy laws were intended to work such a radical change in the nature of local public health and safety regulation — the substitution of government action for citizen compliance — without indication that Congress so intended.

Id. at 921-22 (App. A, 22a). The court of appeals, however, made no specific ruling as to what assets of the estate should be used for compliance purposes. That issue "can properly be resolved only by the bankruptcy court, since the issue was not treated in the proceedings below and so the record on appeal does not include findings of relevant fact." *Id.* at 923 (App. A, 25a).

[6] Because the Long Island City facility constituted such a grave threat to the safety and health of the residents of New York City, after the bankruptcy court authorized abandonment, a cleanup of the tanks and their contents was undertaken at public expense. That cleanup has now been completed. It did not, however, include removal of subsoil contamination. *Quanta*, 739 F.2d at 914 (App. A, 6a).

SUMMARY OF ARGUMENT

Section 554(a) of the Bankruptcy Code does not authorize a bankruptcy trustee to abandon a toxic waste facility where to do so imminently and substantially endangers the environment and public health and safety in violation of federal, state and local laws.

The court below held that the Bankruptcy Code did not preempt state and local public health and safety laws, without addressing whether the proposed abandonment also contravened federal laws. This Court, however, can avoid reaching this constitutional question of preemption by harmonizing two *federal* policies expressed in recent statutes: to protect the health and safety of the American public from toxic wastes, and to provide a fair distribution of debtors' assets among creditors.

Various provisions of the Bankruptcy Code demonstrate that Congress intended bankruptcy trustees as a general matter to comply with federal, state and local public safety laws. Section 554(a) codifies pre-Code law which authorized abandonment only when it does not endanger public safety. This section must also be read together with other provisions of the Code and federal statutes governing trustees. Section 959(b) of the Judicial Code requires a trustee in any cause to comply with valid state laws. Section 362(b)(4) of the Bankruptcy Code exempts post-petition state regulatory enforcement of public safety laws from the automatic stay of all legal proceedings against the debtor even when the grounds for enforcement are rooted in pre-petition conduct. In addition, under section 503(c) of the Bankruptcy Code, expenditure of funds to protect the public from the dangers posed by the toxic waste site is a necessary administrative cost of preserving the estate.

Nothing in the text, legislative history or policy expressed in several statutes passed by Congress in the last decade to protect our environment against hazardous waste products suggests any intention to allow a trustee in bankruptcy to ignore strict regulatory requirements by abandoning a burdensome property. Consequently, state and local laws paralleling these federal

enactments cannot be said to frustrate Congress' objectives in the Bankruptcy Code. Section 554(a) therefore does not preempt otherwise applicable state and local laws for the protection of public health and safety and the environment.

This Court has consistently rejected challenges to legitimate government regulations under the takings clause of the fifth amendment even when the practical effect of compliance would result in complete destruction of the value of the property. The court below properly concluded that limiting the trustee's power to abandon a toxic waste site that was in violation of public safety laws of general applicability, which were in effect at the time the loans were made, did not constitute a taking. The creditors did not have a reasonable, investment-backed expectation that those who operated this toxic waste storage facility would not be required to devote some of their resources to complying with environmental laws.

ARGUMENT

I. A BANKRUPTCY TRUSTEE MAY NOT ENDANGER THE HEALTH AND SAFETY OF MILLIONS OF CITY RESIDENTS BY ABANDONING A STORAGE FACILITY LEAKING TOXIC WASTES, IN VIOLATION OF FEDERAL, STATE AND LOCAL ENVIRONMENTAL STANDARDS.

Federal and state law clearly prohibit what the trustee in bankruptcy here proposed to do: walk away from a dangerous toxic waste facility in the midst of a major metropolitan area, placing large numbers of people in imminent peril of the consequences of leaking PCB's and possible fires. *See* Point I(A), I(B)(iii), *post*. The trustee, however, contends that he is empowered by Congress to endanger the public in this way, even if others are not, because the polluters responsible for the dangerous condition have taken refuge in bankruptcy.

Chiefly, the trustee relies on section 554(a) of the Bankruptcy Code, 11 U.S.C. 554(a) (1982), which provides that:

[a]fter notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

The trustee argues that under this provision the bankruptcy court's inquiry is expressly restricted to whether the property is of inconsequential value or is burdensome to the estate. If the answer is yes, the court must approve abandonment. (T. Br. 13-16). According to the trustee's reading of section 554(a), any violation of a federal, state or local law designed to protect the public safety and the environment, as well as any danger to the public which would occur as a result of abandonment, is of no legal concern to the bankruptcy court.

The United States Court of Appeals for the Third Circuit flatly rejected this argument, finding no support for such a drastic construction of the abandonment provision. Instead, the court of appeals remanded the matter to the bankruptcy court with directions to fashion a solution consistent with the public interest and the requirements of federal and state laws concerning public safety and environmental protection. The State of New York and the City of New York submit that this decision is the only resolution of the matter that is fully consistent with and supported by the various federal and state public safety and environmental laws, the Bankruptcy Code, principles of statutory construction and prior judicial decisions.

A. Federal Environmental and Bankruptcy Laws Should Be Read in Harmony to Protect the Public Safety and the Environment.

In interpreting the limits on the trustee's abandonment power, the court below correctly found that the Bankruptcy Code, taken as a whole, does not preempt state and local laws concerning hazardous waste and designed to protect public health and safety, as we argue more fully below (Point I[B]). This Court, however, need not reach the constitutional preemption question because, we argue below, the abandonment of a facility containing hundreds of thousands of gallons of hazardous wastes violates a broad

range of *federal* environmental protection statutes, as well as parallel state and local laws.[7]

The need to accommodate the directives of different federal laws, of course, does not present supremacy clause questions. Rather, it presents a question of harmonization. The basic rule of statutory construction is that:

> [W]here two statutes are " 'capable of co-existence, it is the duty of the courts, absent a clearly expressed congressional intention to the contrary, to regard each as effective.' " *Regional Rail Reorganization Act Cases*, 419 U.S., at 133-134, 95 S.Ct. at 353-354, quoting *Morton v. Mancari*, 417 U.S. 535, 551, 94 S.Ct. 2474, 2483, 41 L.Ed.2d 290 (1974).

Ruckelshaus v. Monsanto, 104 S. Ct. 2862, 2881 (1984).

Here, no evidence has been produced of any congressional intent that the abandonment power of a trustee in bankruptcy under section 554(a) overrides the requirement of compliance with federal environmental laws, particularly those comprehensive laws that were passed or substantially amended since the Bankruptcy Code was enacted in 1978. Moreover, the purposes of the Bankruptcy Code and the purposes of the federal environmental protection laws are not mutually exclusive or antagonistic. As is discussed more fully below, Congress intended these two purposes to be harmonized.

Broadly viewed, the historic purpose of the federal bankruptcy statues is to bring about an equitable distribution of the bankrupt's estate among creditors "holding just demands based upon adequate consideration." *Kothe v. R.C. Taylor Trust*, 280 U.S. 224, 227 (1930). Environmental regulation is a more recent concern of the federal government. Reflecting a growing anxiety about the grave threat hazardous chemicals pose to the public

[7] The State of New York argued in the courts below that the trustee's actions violated federal as well as state and local laws. *See, e.g.*, Brief of Appellants in the Court of Appeals for the Third Circuit at 5, 7-10, 12, 14, 23. The court of appeals did not directly address this point.

health and the environment, Congress in the past ten years has enacted several new statutes and amended existing statutes in order better to control this toxic threat.[8]

[8] During the past decade, Congress has enacted or amended the following environmental protection laws:

a. Toxic Substances Control Act (TSCA), 15 U.S.C. § 2601 *et seq.* (enacted 1976, most recently amended 1984). In enacting TSCA, Congress declared that it was "the policy of the United States that . . . adequate authority should exist to regulate chemical substances and mixtures which present an unreasonable risk of injury to health or the environment, and to take action with respect to chemical substances and mixtures which are imminent hazards. . . ." 15 U.S.C. § 2601(b) (1982). As the Senate Report makes clear, Congress intended TSCA to be "a comprehensive measure to protect the public and the environment from exposure to hazardous chemicals." S.Rep. No. 698, 94th Cong., 2d Sess. 3, *reprinted in* 1976 U.S. Code Cong. & Ad. News 4491, 4493. The Senate Report demonstrates that Congress was particularly concerned about the dangers of PCB's, *id.* at 3-4, 1976 U.S. Code Cong. & Ad. News at 4493-94, and that Congress considered "controlling toxic chemicals in the environment is one of the crucial health requirements facing this nation." *Id.* at 4, 1976 U.S. Code Cong. & Ad. News at 4494.

b. Comprehensive Environmental Response, Compensation and Liability Act (CERCLA), 42 U.S.C. § 9601 *et seq.* (enacted 1980, most recently amended 1984). In passing this "Superfund" legislation known as CERCLA, Congress sought in part to address the problem of inactive hazardous waste sites which in the past "have forced state and local governments to bear the costs" of cleanup. H.R. Rep. No. 1016, Part I, 96th Cong., 2d Sess. 20, *reprinted in* 1980 U.S. Code Cong. & Ad. News 6119, 6123.

c. Federal Water Pollution Control Act (Clean Water Act), 33 U.S.C. § 1251 *et seq.* (enacted 1948, most recently amended 1984). In passing the Clean Water Act, Congress announced a strong "national policy that discharge of toxic pollutants in toxic amounts be prohibited." 33 U.S.C. 1251(a)(3) (1982). The Senate Committee on Public Works conducted a two-year study of the existing federal water control program and concluded that "the national effort to abate and control water pollution has been inadequate in every vital aspect," S.Rep. No. 414, 92d Cong., 2d Sess. 7, *reprinted in* 1972 U.S. Code Cong. & Ad. News 3668, 3674, and proposed a major change in the enforcement mechanism to increase the federal role. *Id.*, 1972 U.S. Code Cong. & Ad. News at 3675.

d. Resource Conservation and Recovery Act (RCRA), 42 U.S.C. § 6901 *et seq.* (enacted 1976, most recently amended 1984).

e. Clean Air Act, 42 U.S.C. § 7401 *et seq.* (enacted 1955, most recently amended 1982).

The Long Island City toxic waste site is a facility governed by the Comprehensive Environmental Response, Compensation and Liability Act of 1980, 42 U.S.C. § 9601(9)(1982). Under CERCLA, *any* person who disposes of hazardous waste at such a facility is liable for cleanup costs and damages. 42 U.S.C. § 9607(a) (1982). The debtor's estate and the trustee in his representative capacity are such "persons" under CERCLA. 42 U.S.C § 9601 (21)(1982). *See also In re T.P. Long Chemical, Inc.*, 45 Bankr. 278 (Bankr. N.D. Ohio 1985). The trustee cannot shift the liability of the estate to a third party. 42 U.S.C. § 9607(e)(1) (1982).

Abandonment of PCB-contaminated waste oil would also violate the Toxic Substances Control Act (TSCA) and regulations which explicitly prescribe the proper disposal of PCB's.[9] Pursuant to regulations, PCB-contaminated materials, depending on their concentration levels, must either be disposed of in special landfills or destroyed in approved incinerators. 40 C.F.R. § 761.60 *et seq.* (1984). The Environmental Protection Administration ("EPA") promulgated these comprehensive regulations after determining that "the manufacture, processing, and distribution in commerce of PCB's . . . presents an unreasonable risk of injury to health within the United States . . . based upon the well-documented human health and environmental hazard of PCB exposure." 40 C.F.R. § 761.20 (1984). Abandoning such highly toxic substances in the heart of New York City is clearly prohibited under TSCA.

In addition, abandonment of the Long Island City facility violated the imminent hazard provisions of the Resource Conservation and Recovery Act (RCRA) in effect at the time of the bankruptcy court's order, 42 U.S.C. § 6973 (1982), as well as those added in the 1984 amendments to the Act. 42 U.S.C.A. § 6972 (West Supp. 1985). Finally, the trustee's actions implicated the Clean Water Act's prohibition against discharges of hazardous substances into navigable waters. 33 U.S.C. § 1321(b)(3) (1982).

[9] Because of the particular dangers posed to the public health and the environment by PCB's, they are the only class of chemicals which Congress has specifically addressed in a statute, rather than leaving them for regulation by EPA under its general authority to regulate toxic substances. *See* 15 U.S.C. §2605(e)(1982).

Under the Clean Water Act, the trustee cannot shift liability to a third party not responsible for the discharge. 33 U.S.C. § 1321(f),(g) (1982).

None of these comprehensive federal enactments expressly exempts from its requirements a trustee in bankruptcy seeking to abandon burdensome property. Legislative history fails to disclose any such congressional intention. Logic, too, suggests that the poisoning of our environment would not be considered benign or acceptable to Congress because it was done in order to preserve the assets of creditors. Congress was surely aware that requiring facilities which stored deadly substances to be maintained and monitored might diminish or even eliminate the creditor's security. It nonetheless gave higher priority to avoiding the costs and permanent consequences to the environment and public health and safety which would result from the dumping of indefinitely life-endangering substances.

Congress has not held the view, shared by the bankruptcy court below and the trustee, that cities and states should bear the financial responsibility for disposal and cleanup of hazardous chemicals generated by private parties. At the time of CERCLA's passage, Congress was aware that "EPA estimated that as many as 30,000 to 50,000 inactive and uncontrolled hazardous waste sites existed in the United States, and estimated that cleanup of the 1200 to 2000 most dangerous sites alone would cost between $13.1 and $22 billion. H.R. Rep. No. 1016, 96th Cong., 2d Sess. 18, 20 (1980), *reprinted in* 1980 U.S. Code Cong. & Ad. News 6120, 6123." *State of New York v. General Electric*, 592 F. Supp. 291, 302 n.21 (N.D.N.Y. 1984). Because Congress believed existing hazardous waste sites should not be cleaned up by public funds alone, it decreed that generators and transporters of hazardous chemicals, as well as owners and operators of property in which hazardous chemicals were stored or disposed of, were liable for cleanup costs, irrespective of the "Superfund" created by CERCLA. *State of New York v. General Electric*, 592 F.Supp. at 302; *United States v. Reilly Tar & Chemical Corp.*, 546 F.Supp 1100, 1112 (D. Minn. 1982).

Similarly, in broadening the citizens suit provision in RCRA in the 1984 amendments to that Act, Congress expressly recognized

that the government cannot be expected to be responsible to clean up all hazardous waste sites. In the report accompanying the amendments, the House Energy and Commerce Committee stated:

> The Committee believes this expansion of the citizens suit provision will complement, rather than conflict with, the Administrator's efforts to eliminate threats as to the public health and the environment, *particularly where the Government is unable to take action because of inadequate resources.*

H.R. Rep. No. 198, Part I, 98th Cong., 2d Sess. 53 , *reprinted in* 1984 U.S. Code Cong. & Ad. News 5576, 5612 (emphasis supplied). Surely, therefore, Congress did not intend government to step in and finance remediation of additional hazardous waste sites created by newly bankrupt companies when responsible parties were on the scene.

New York has been vigorous in enforcing these federal statutes.[10] Indeed, the Court of Appeals for the Second Circuit has recently affirmed the State's authority to obtain injunctive relief under state law and "response costs" under CERCLA for cleaning up a hazardous waste storage facility. *State of New York v. Shore Realty Corp.*, No. 84-7925, slip op. at 3065 (2d Cir. Apr. 4, 1985). New York was here seeking to remedy similar violations of both federal and state law. *See* n.7, *ante*.

B. The Trustee's Power to Abandon Under Section 554(a) Is Limited by Requirements of Public Safety.

The trustee points to the seemingly unqualified language of section 554(a) as authorizing him to abandon the Quanta facility

[10] New York has additional authority to enforce federal environmental laws under its *parens patriae* power. It has frequently done so because it has "a quasi-sovereign interest in the health and well-being—both physical and economic—of its residents in general." *Alfred L. Snapp & Son, Inc. v. Puerto Rico ex rel. Baez*, 102 S. Ct. 3260, 3269 (1982); *People by Abrams v. 11 Cornwell Company*, 695 F.2d 34, 38 (2d Cir. 1982). In addition, the environmental laws create benefits and alleviate hardships which the "state will obviously wish to have accrue to its residents." *Snapp*, 102 S. Ct. at 3269; *11 Cornwell*, 695 F.2d at 39. *See also Maryland v. Louisiana*, 451 U.S. 725 (1981); *Georgia v. Pennsylvania R. Co.*, 324 U.S. 439 (1945).

without regard to the requirements of recently enacted environmental safeguards. Whenever the policies of the Bankruptcy Code come into possible conflict with other federal policies, this Court has made clear the judiciary's function is to harmonize them. *See, e.g., National Labor Relations Board v. Bildisco*, 104 S. Ct. 1188, 1197 (1984); *see also In re Nitec Paper Corp.*, 43 Bankr. 492, 499 (S.D.N.Y. 1984); *In re Kish*, 41 Bankr. 620, 626 n.6 (Bankr. E.D. Mich. 1984); *In re Kennise Diversified Corp.*, 34 Bankr. 237, 245 (Bankr. S.D.N.Y. 1983). A trustee's abandonment power has never been so broadly construed as to sanction overriding of laws enacted for public health and safety, as a review of the case law leading to enactment of 11 U.S.C. § 554(a) (1982) indicates.

The provisions of the Code, read together, demonstrate a congressional intent that trustees in bankruptcy are to comply with laws designed to protect public health, safety and the environment. For example, section 554(a) is properly seen as having codified the "public endangerment" exception judicially developed prior to its enactment. Furthermore, the trustee's authority to abandon is subject to his duty to manage and operate the property in accordance with state law. 28 U.S.C. § 959(b) (1982). Likewise, there is an exception in 11 U.S.C. § 362(b)(4) (1982) to the automatic stay of all proceedings against the bankrupt for governmental enforcement actions. All evidence a clear congressional intention that bankruptcy concerns be accomodated with other important societal interests.

i. The Trustee's Authority to Abandon Is Subject to Health and Safety Laws.

Cases decided prior to the 1978 enactment of section 554(a) plainly recognize that a trustee's ability to abandon property has historically been subject to the requirements of public health and safety. Absent some indication of a contrary intent — and the legislative history of section 554(a) is silent on this — the proper conclusion to be drawn is that section 554(a) codifies the rule established in such cases as *Ottenheimer v. Whitaker*, 198 F.2d 289 (4th Cir. 1952), and *In re Lewis Jones, Inc.*, 1 Bankr. Ct. Dec. 277 (Bankr. E.D.Pa. 1974), that a trustee may not abandon

property where doing so would endanger public health and safety.[11] L. King, 4 *Collier on Bankruptcy* ¶554.01 at 554-5 (15th ed. 1985) ("This section [554(a)] makes few substantive changes in prior law, but seeks to clarify certain ambiguities and to codify cases resulting from legislative silence on the matter."); *accord*, Editorial Commentary and Analysis, Bankr. Serv. L. Ed. § 23:111 (1979). The judge-made law which section 554 codifies demonstrates quite plainly that although a trustee's power to abandon burdensome or worthless property was recognized by the courts long before the codification at 11 U.S.C. § 554(a) in 1978, "the exercise of the power to abandon is subject to the application of general regulations of a police nature."[12] L. King, 4A *Collier on Bankruptcy* ¶70.42(2) at 502-04 (14th ed. 1978).

In *Ottenheimer v. Whitaker*, the trustee in bankruptcy petitioned the court for leave to abandon, as burdensome to the estate,

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[11] Because the legislative history is silent, it is appropriate to consult these decisions in the interpretation of the codification in section 554(a). N. Singer, 2A *Sutherland Statutory Construction* § 48.03 at 291 (4th ed. 1984). *See also National Labor Relations Board v. Amax Coal Co.*, 453 U.S. 322, 329 (1980).

[12] The trustee argues that because Congress did not write into the section 554(a) abandonment power a "public endangerment" rule, it therefore intended to reject the judge-made rule, citing *National Labor Relations Board v. Bildisco*, 104 S. Ct. 1188 (1984) (T. Br. 15-16). The short answer is that there was no need to reiterate such a rule because, as we demonstrate below, 28 U.S.C. § 959(b) and 11 U.S.C. § 362(b)(4) limit the trustee's authority to abandon under section 554(a) and, in combination, mandate a "public endangerment" rule. Nonetheless, the Court's statement in that case that "Congress knew how to draft an exclusion . . . when it wanted to," 104 S. Ct. at 1195, here undermines the trustee's position. When Congress directed bankruptcy trustees in section 959(b) to manage and operate the property in accordance with state law, it provided an exemption for railroad reorganizations but none that would apply to the present case. When Congress decided not to stay automatically governmental enforcement proceedings once a petition is filed, it did not specify an exception for proposed abandonment by a trustee. 11 U.S.C. § 362(b)(4). When Congress wrote the numerous environmental laws discussed above, it could have excepted trustees in bankruptcy, either in general or only when they propose to abandon property, but did not do so, even though it did enumerate other exceptions to the coverage of those laws. *See, e.g.*, 42 U.S.C. § 9607(b) (1982) (defenses to CERCLA).

certain floating barges. The abandonment was opposed by the Harbor Engineer of Baltimore and the United States Army Corps of Engineers on the ground that the proposed abandonment would violate 33 U.S.C. § 409 (1982) (Act of Mar. 3, 1899), which made it unlawful to sink vessels in navigable channels. Testimony had shown that the barges were in dilapidated condition and, if abandoned, would sink at anchorage. The court not only denied the trustee permission to abandon the barges but directed him to remove them from the anchorage and mandated that the cost of removal be borne by the bankrupt estate as a cost of administration. The court of appeals declared that the well-settled rule that a trustee can refuse to accept property of an onerous or unprofitable nature would have applied were it not for the unusual consequences that would follow:

> There can be no doubt that the property not only has no value, but also that the care and disposition of it will involve the expenditure of a substantial sum of money. But it is equally true that if the trustee abandons the barges *and at the same time holds on to the valuable assets of the estate, the title to the barges will revert to the bankrupt and he will be left without means to care for or dispose of them in the manner prescribed by the statute.*

198 F.2d at 290 (emphasis added).

The Bankruptcy Court for the Eastern District of Pennsylvania reached a similar result in *In re Lewis Jones, Inc.*, 1 Bankr. Ct. Dec. 277 (Bankr. E.D. Pa. 1974). In that case, the trustees of three bankrupt utility companies sought instructions from the court concerning certain underground manholes, vents and steam pipes which could become hazardous to public health and safety if abandoned in their existing condition. These structures could be made safe by repaving, filling and sealing but only at a very substantial cost. In *Lewis Jones*, unlike in *Ottenheimer* or the present case, no federal or state statute would have been violated had the trustee not spent the money to remove the potential hazard. Nevertheless, despite the cost involved for the estate, the court ordered the trustees to remedy the potentially hazardous

condition, finding that "even absent the violation of a state or federal act, the public interest must be protected by the Bankruptcy Court." *Lewis Jones*, 1 Bankr. Ct. Dec. at 280. The *Lewis Jones* court relied, as did the court below, upon the principle announced in *Securities and Exchange Commission v. United States Realty & Improvement Co.*, 310 U.S. 434, 455 (1940):

> A bankruptcy court is a court of equity and is guided by equitable doctrines and principles except as they are inconsistent with the Act. A court of equity may in its discretion in the exercise of the jurisdiction committed to it grant or deny relief upon performance of a condition which will safeguard the public interest. (citations omitted).

There is no indication that in codifying the abandonment power, Congress intended to eliminate the judicially evolved "public endangerment" exception. Indeed, it was recently reaffirmed in *In re T.P. Long Chemical Co.*, 45 Bankr. 278 (Bankr. N.D. Ohio 1985). Adopting the same reasoning as the court below, the bankruptcy court held that section 554(a) did not authorize a trustee to abandon barrels of hazardous materials. The court stated that "the congressional policy underlying CERCLA is that those who generate, use, or transport hazardous materials should be required to pay the cost of damages caused by the hazardous materials" and that "the estate cannot avoid the liability imposed by CERCLA." 45 Bankr. at 286. Similarly, in *In re 30 Hill Top Street Corp.*, 42 Bankr. 517, 519-520 (Bankr. D. Mass. 1984), the court denied the trustee's motion to abandon a nursing home in a Chapter 7 case where the proposed abandonment would return the property to the debtor, who was in no position to correct the deficiencies in health care services which threatened the health and safety of the patients.

ii. Requiring the Trustee to Manage the Estate in Compliance with Federal and State Environmental Laws Is Consistent with *Ohio v. Kovacs*.

In *Ohio v. Kovacs*, 105 S.Ct. 705 (1985), this Court held that the obligation of an individual debtor to comply with a state

court injunction, which was issued prior to the filing of a bankruptcy petition and required him to clean up a toxic waste dump, had been converted into an obligation to pay money dischargeable in bankruptcy when the individual debtor had been relieved of his property by a receiver *prior* to the bankruptcy. Kovacs was therefore unable to satisfy the obligation to clean up the site other than by a payment of money, even before the bankruptcy petition was filed. 105 S. Ct. at 710-711. Here, by contrast, the state is seeking to enforce the post-petition obligation of the trustee in charge of the site not to take steps which violate federal and state environmental laws designed to protect the public. (The trustee concedes that "[t]he states are free to direct future conduct of debtors and debtors-in-possession. . . ." (T. Br. 35).).

This Court, in reaching the decision in *Kovacs*, was careful to limit its holding to the narrow issue presented. It declared that it did not question that anyone in possession of the site, including a trustee in bankruptcy, must comply with the state's environmental laws. 105 S. Ct. at 711-12. Likewise, the Court further stated in *Kovacs* that it was *not* holding that "the injunction against bringing further toxic wastes on the premises or *against any conduct that will contribute to the pollution* of the site or the State's waters is dischargeable in bankruptcy," 105 S.Ct. at 711 (emphasis supplied), and, citing *Penn Terra, Ltd. v. Department of Environmental Resources*, 733 F.2d 267 (3d Cir. 1984), noted that the automatic stay provision of section 362(a) "does not apply to suits to enforce the regulatory statutes of the State." *Kovacs*, 105 S.Ct. at 711 n.11.[13] Thus, *Kovacs* did not relieve the trustee,

[13] This conclusion is consistent with other lower court decisions refusing to stay regulatory injunctions and license revocations regulating future conduct of the debtor, even when the grounds for such enforcement arose before bankruptcy. *See, e.g., In re Thomassen*, 15 Bankr. 907 (Bankr. 9th Cir. 1981) (permitting administrative proceedings which could have resulted in revocation of debtor physician's license on the basis of pre-bankruptcy professional negligence); *Commodities Futures Trading Commission v. Incomco, Inc.*, 649 F.2d 128 (2d Cir. 1981) (permitting regulatory enforcement proceeding seeking to enjoin activities in the commodities market on the basis of pre-bankruptcy violations); *In re D.H.*

(Footnote Continued)

as the person in possession of the hazardous waste dump for nearly eight months, of an obligation to manage the site without risking harm to the public and not to endanger the public further by abandoning it in violation of federal or state law.[14]

iii. Section 959(b) Requires the Trustee to Comply with Public Health and Safety Requirements When Managing and Abandoning Property.

Section 959(b) of the Judicial Code requires the trustee to "manage and operate the property" according to state law. The trustee argues that because of section 554(a) he could jettison any obligation to obey state laws by abandoning the property. New York contends, to the contrary, that in view of the history of judicially established limitations on the trustee's power to abandon, section 554(a)'s conferral of that power is to be read *in pari materia* with the basic obligation of the trustee under federal law to manage and operate the property consistently with state law requirements. 28 U.S.C. § 959(b).[15]

(Footnote Continued)

Overmeyer Telecasting Co., Inc., 35 Bankr. 400 (N.D. Ohio 1983) (permitting FCC proceedings to suspend debtor's broadcasting license); *In re Kennise Diversified Corp.*, 34 Bankr. 237, 243 (Bankr. S.D.N.Y. 1983) (permitting housing authority to correct serious housing code violations endangering tenants although debtor landlord's conduct was rooted in pre-petition period).

[14] This Court never addressed in *Kovacs* whether the trustee could simply abandon a currently dangerous toxic dump to an insolvent debtor without making provisions to protect the public. In *dicta*, this Court merely noted that section 554(a) authorizes abandonment of valueless property, but it did not have occasion to determine the scope of the public endangerment exception codified in that section. 105 S.Ct. at 711 n.12. There was no finding in *Kovacs* that the toxic dump at the time of bankruptcy posed the imminent danger presented here.

[15] *In re Kennise Diversified Corp.*, 34 Bankr. 237, 243 (Bankr. S.D.N.Y. 1983), provides support for this analysis. In that case, the court declared that "Bankruptcy Code § 362(b)(4) and 28 U.S.C. § 959 form a smooth continuum and make it apparent that Kennise as debtor in possession must operate its building according to the dictates of non-bankruptcy law that would apply if there were no Chapter 11 case." *See also In re Briarcliff*, 15 Bankr. 864, 868 (D.N.J. 1981) (holding that the exemption from the automatic stay provision in section 362(b)(4) must be read together with section 959).

There is no question that the abandonment of half a million gallons of flammable liquids, much of it contaminated with dangerous PCB's, in the middle of New York City violates New York law. In fact, it is a felony. N.Y. Envtl. Conserv. Law ("ECL") 71-2713 (McKinney 1984). *See also* ECL §§27-0701, 0914; 71-2711, 2712 (McKinney 1984); *State of New York v. Shore Realty Corp.*, slip op. at 3099 (public nuisance). In effect, the trustee acknowledges that by virtue of section 959(b) he would be bound by New York's environmental laws if Quanta were in reorganization (T. Br. 23), but he maintains that section 959(b) applies only in a reorganization, not in a liquidation.[16] There is no support for this narrow reading in the text of section 959(b), its legislative history, judicial interpretation or logic.

First, on its face section 959(b) applies to a trustee "appointed in *any* cause pending in *any* court of the United States." 28 U.S.C. §959(b)(1982)(emphasis supplied). The *only* exception is "as provided in section 1166," *id.*, which governs railroad reorganization proceedings and is inapplicable here; under well-settled principles of statutory construction, "[t]he enumeration of exclusions from the operation of a statute indicates that the statute should apply to all cases not specifically excluded." N. Singer, 2A *Sutherland Statutory Construction* §47.23 at 194 (4th ed. 1984). No distinction is made in the language of the statute between managing a reorganization and managing an orderly liquidation. In fact, Congress clearly envisioned the trustee managing and operating a business under Chapter 7 because 11 U.S.C. § 721 (1982) authorizes such activity by the trustee.

There is, likewise, nothing in the legislative history indicating that section 959(b) applies only in a reorganization. Courts other than the court below have held section 959(b) applicable to trustees managing property in liquidations. For example, in *In re 30 Hill Top Street Corp.* the court held that a trustee operating

[16] The court of appeals determined that even if section 959(b) does not by itself require compliance with state and local law governing hazardous waste facilities, as New York believes it does, section 959(b) assuredly does provide more evidence that Congress did not intend the Bankruptcy Code to preempt state and local police power governing safety and health. 739 F.2d at 919 (App. A, 17a).

a nursing home in a Chapter 7 case pursuant to the trustee's section 721 power to operate a business during liquidation was obligated under section 959 to comply with state law. Similarly, the court in *In re Charles George Land Reclamation Trust*, 30 Bankr. 918 (Bankr. D. Mass. 1983), held that a trustee in a Chapter 7 liquidation case must manage a hazardous waste site in compliance with state law and protect the public from leaking toxic wastes. *See also In re Briarcliff*, 15 Bankr. 864, 868 (D.N.J. 1981) (*dictum* that trustees in any case are obligated under section 959 as officers of the court "to comply with applicable State and local law while they carry on their activities").

Likewise, there is not the slightest support in policy or logic for the anomalous interpretation advanced by the trustee. Adoption of the trustee's reasoning would lead to the peculiar result that a trustee is required to comply with state environmental laws while administering the estate under a Chapter 11 reorganization case, but is free from such restrictions if the estate is converted to a Chapter 7 case. This would provide an obvious incentive for unscrupulous debtors and creditors to seek to convert reorganization cases to Chapter 7 cases. Encouraging such hazardous enterprises to go into liquidation in order to avoid compliance with environmental laws is precisely the opposite of what Congress intended.

Moreover, the logic of the cases discussed below, applying section 959(b) to require trustees in reorganization cases to comply with state laws regardless of financial consequences, is equally compelling in a Chapter 7 liquidation case where no hope remains of salvaging a business. In each of these cases, where the actions of the debtor in possession, trustee or receiver would or could have caused injury to the public or the environment, the court held that the police and regulatory powers of the state took precedence, even where such regulations might affect the rehabilitation of the debtor and result in significant reduction of its assets.

In *Gillis v. California*, 293 U.S. 62 (1934), this Court rejected the receiver's request to be relieved of compliance with a California licensing law, even though without such relief the

reorganization would fail. In *In re Dolly Madison Industries*, 504 F.2d 499 (3d Cir. 1974), the court upheld the revocation of a certificate to do business by the State of Virginia for failure of a business in reorganization to pay a registration fee and file annual reports. In *In re Nitec Paper Corp.*, 43 Bankr. 492 (S.D.N.Y. 1984), the court held that under section 959, "[a] reorganization must be formulated within the bounds of existing state and federal law." *Id.* at 499 (footnote omitted). The courts in *In re Briarcliff* and *In re Kennise Diversified Corp.* reached similar results. The court in *In re Canarico Quarries, Inc.*, 466 F.Supp. 1333 (D.P.R. 1979), required a corporation in Chapter XI to comply with the requirements of the Puerto Rican Environmental Quality Board, by ceasing emissions in violation of the Federal Clean Air Act, even if such compliance required the closing of the business, thereby defeating the purposes of the attempted arrangement. *See also Colonial Tavern, Inc. v. Byrne*, 420 F.Supp. 44 (D. Mass. 1976) (suspension of liquor license upheld for repeated violations of midnight closing hour regulations); *In re Grand Spaulding Dodge, Inc.*, 5 Bankr. 481 (N.D. Ill. 1981) (suspension of automobile dealership license due to fraud upheld, citing in part 28 U.S.C. § 959(b)); *Commonwealth v. Peggs Run Coal Co.*, 55 Pa. Commw. 312, 423 A.2d 765 (1980) (permitting the state to close a coal production facility which was violating local environmental laws).[17]

[17] This analysis of section 959(b) is consistent with the interpretation given by some courts to the narrower limitation in section 959(a) providing that trustees "may be sued . . . with respect to any of their acts or transactions in carrying on business connected with such property." 28 U.S.C. §959(a)(1982). These courts have permitted suits against trustees under section 959(a) for tortious acts committed by trustees during liquidation or reorganization which have harmed members of the public, while carefully distinguishing such suits, which do not affect the title, possession, control, liquidation or distribution of the assets, from those which directly interfere with administration of the estate. *See, e.g., In re 30 Hill Top Street Corp.* (trustee in Chapter 7 liquidation operating nursing home obligated under section 959(a) to comply with state public safety laws); *McGreavey v. Straw*, 90 N.H. 130, 138, 5 A.2d 270, 276 (1939).

The *sole* authority cited by the trustee before this Court (T. Br. 22-23)[18] in support of his contention that section 959(b) does not govern the activities of trustees in liquidation cases is a statement in J. Moore, 7-Pt. 2 *Moore's Federal Practice*, ¶66.04(4) at 1913 (2d ed. 1984), concerning whether state laws regulating distribution of funds in receivership must be followed:

> §959(b) applies only to the receiver in the operation of property in his possession. It does not apply to the distribution of the estate, and does not require the federal receivership court to comply with state laws regulating distribution of funds in receivership, although *Erie R. Co v. Tompkins* should now require it to do so in cases involving only non-federal matters. (footnotes omitted).

Clearly, the treatise does not address whether state health and safety or other police regulations must be followed in a liquidation case. Rather, it is discussing whether state or federal laws would govern when the only question concerns the *distribution of assets*. As the last clause of the quoted language indicates, Prof. Moore's treatise is not authority for the proposition that the trustee need not comply with state environmental laws in a liquidation case.

Given that section 959(b) "is a clear indication that in general the congressional scheme was not intended to subjugate state and local regulatory laws," *Quanta*, 739 F.2d at 919 (App. A, 17a), there is simply no justification to limit artificially the broad term

[18] The trustee has properly abandoned his reliance on *dicta* in a footnote in *State of Missouri v. United States Bankruptcy Court*, 647 F.2d 768, 778 n.18 (8th Cir. 1981), *cert. denied*, 454 U.S. 1162 (1982). In that case, the court indicated a "doubt" that the trustee would have to obtain a state license to sell grain if the company were liquidating rather than reorganizing. The court cites no authority for this proposition. Moreover, as the court below indicated, *Quanta*, 739 F.2d at 920 (App. A, 18a), had the trustee proposed to enhance the estate by selling contaminated grain in violation of state law, regardless of threats to health and safety, it is unlikely the Eighth Circuit would have entertained doubts.

"management"[19] in section 959(b) to exclude the trustee's proposed abandonment of burdensome property. Abandonment of burdensome property is plainly an act undertaken by the trustee to "manage and operate the property" of the estate.[20] Under section 959(b), it must therefore be done in conformity with state law. This obvious reading permits the trustee's authority to abandon property under 11 U.S.C. § 554(a) to be readily harmonized with the strictures of both federal and state environmental laws. It also makes evident sense. There is no reason to believe that Congress wished to allow terminally ill businesses, unlike those on the critical list, to expire in derogation of state law. Finally, this construction of section 959(b) is compelling because it obviates the need for a constitutional determination as to whether section 554(a) preempts state and local environmental laws.

iv. To Deprive State and Local Governments of the Ability to Prevent Threatened Disposals of Dangerous Hazardous Waste Is Inconsistent with Congressional Intent.

State and local governments must always have, under their police powers, the ability to forestall imminent peril to their general populace by doing what New York here sought to do: obtain a remedial court order addressed to a demonstrable threat in the near term to public health, safety and the environment. To hold otherwise is, we fear, to imperil the public, despite the plain intent of Congress to lessen the perils posed by toxic waste facilities. It also is to extend an open invitation to the unscrupulous to use the bankruptcy courts to avoid the stringent requirements of recently enacted environmental laws.

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[19] Webster's Third New International Dictionary (1976) defines management as "the act or art of managing . . . the conducting or supervising of something . . . directing, controlling, and supervising any industrial or business project or activity with responsibility for results . . . judicious use of means to accomplish an end . . . skillful . . . treatment . . . ."

[20] Although the court of appeals indicated it believed this construction of section 959(b) "would seem open to question," it stated further that "[i]t would not strain the language to construe 'management of the property' to include abandonment of a facility." *Quanta*, 739 F.2d at 919 (App. A, 17a).

This obvious concern must have been what prompted this Court in *Ohio v. Kovacs* to caution what it was *not* declaring: that the filing of a petition in bankruptcy excuses a pre-existing duty not to dispose of toxic wastes improperly, or relieves the trustee of the need to comply with environmental laws. 105 S.Ct. at 711. In the present proceeding, this Court ought not render local authorities impotent to protect health and safety against a palpably awesome menace, such as was posed by the Quanta site, absent the clearest indication that Congress intended such an extensive evisceration of traditional local regulatory authority. Plainly, no such indication has been provided.

Rather, as the court of appeals found, 739 F.2d at 918 (App. A, 15a), the contrary intent appears from Congress' enactment of an exception to the automatic stay provision of the Bankruptcy Code for "the commencement or continuation of an action or proceeding by a governmental unit to enforce such governmental unit's police or regulatory power." 11 U.S.C. § 362(b)(4); *see also* 28 U.S.C.A. § 1452 (West Supp. 1985) (limiting removal of actions by governmental units to enforce police or regulatory authority). The Senate's Report on this provision expressly contemplated its application to suits concerning environmental protection laws. S. Rep. No. 989, 95th Cong., 2d Sess. 52, *reprinted in* 1978 U.S. Code Cong. & Ad. News 5787, 5838. This exception to the general rule staying legal proceedings against the debtor is persuasive evidence that Congress did not envision state and local governments being powerless to use their "police or regulatory power" to protect public safety, health and the environment when those are threatened by such proposed actions of a trustee as abandonment of a toxic waste facility.

The trustee argues, however, that in abandoning Quanta's storage facility containing hazardous, flammable liquids he has taken no affirmative act, but has merely divested the estate of title to the property so that it is revested in the debtor corporation. (T. Br. 24). In short, he argues, abandonment is not really disposal. The trustee's argument is factually and legally incorrect.

First, as shown above, by removing guards and supervisory personnel, shutting down the fire suppression system and leaving

hazardous wastes leaking from an unattended facility, the trustee created a new, highly dangerous situation which cannot be attributed to the acts of the debtor. The trustee's analysis of the import of his activities in abandoning this property may apply to innocuous, static property posing no public risk; it is, however, woefully deficient where federal, state and local laws recognize that the proper maintenance and handling of such property is perpetually a matter of grave public concern. To abandon or fail to maintain a dangerous waste facility is to *create* a hazard to the community, for hazardous waste which is separated from the equipment, supervision and resources necessary to control its destructive potential is radically different from hazardous waste which is stored, supervised and disposed of properly.

If the property of the estate included not a toxic waste facility but rather a zoo full of sick animals which, because of their diseased condition, could not be sold, the trustee would surely not be empowered to sell the cages, fire the caretakers and abandon those dangerous animals, separating them from the personnel, equipment and other resources necessary to control them. By the same token, a trustee surely would not be permitted to strip a nuclear power plant of its salable items of equipment, dismiss the personnel and abandon the uncontrolled reactor, with the excuse that it was the debtor who had started the chain reaction many years earlier. It is the very act of removing the assets necessary to control the hazardous waste that creates the danger to the community.

The trustee's argument is legally flawed as well. The United States Court of Appeals for the Fourth Circuit rejected such an active-passive distinction in interpreting disposal of hazardous wastes pursuant to RCRA, 42 U.S.C. § 6973 (1982). In *United States v. Waste Industries, Inc.*, 734 F.2d 159, 164 (4th Cir. 1984), the court stated:

> [A] strained reading of that term ["disposal"]limiting its section 7003 meaning to active conduct would so frustrate the remedial purpose of the Act as to make it meaningless. Section 7003, unlike the provisions of the Act's subtitle C, does not regulate conduct but regulates and mitigates endangerments. The Administrator's intervention authorized by section 7003 is triggered by evidence that the "disposal of ... hazardous waste *may present* an imminent and substantial endangerment." (emphasis supplied by court).

The trustee's argument that the only consequence of his action is that the hazardous waste reverts to the debtor sidesteps the critical fact that he has removed all assets from the debtor. The Third Circuit properly recognized that an act which separates hazardous waste from the assets necessary to check its destructive potential constituted final disposal of the hazardous waste which "clearly contravened applicable law, and did so not merely technically, but with severely deleterious implications for the public safety." *Quanta*, 739 F.2d at 921 (App. A, 21a). To say, as the trustee does, that the debtor corporation is now responsible for the hazardous waste is to engage in dangerous fiction because the debtor has been reduced to a paper entity without assets.[21]

Finally, the trustee makes a fundamental error in characterizing New York as a creditor seeking to obtain a priority status not otherwise provided for in the Bankruptcy Code. In June of 1981, when the City and State of New York appeared in bankruptcy court to oppose the trustee's effort to abandon the Long Island City facility, they did so not as creditors, for in fact nothing was owed financially by the debtor to New York. Rather, the City and State appeared in order to inform the court that abandonment of hazardous wastes, the act for which the trustee sought court approval, would create a grave danger to the health and safety of the public and violate federal, state and local environmental laws. It was only as a result of the bankruptcy court's

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[21] Indeed, a further distinction between Kovacs and this case is that debts of individual debtors such as Kovacs are dischargeable in bankruptcy, 11 U.S.C. § 727 (1982), whereas those of a corporate debtor such as Quanta are not. *Id.* Congress eliminated dischargeability of corporations because it assumed that corporations would be empty shells and it wanted to "avoid trafficking in corporate shells." H.R.Rep. No. 595, 95th Cong., 1st Sess. 384, 1978 U.S. Code Cong. & Ad. News 5787, 6340.

erroneous determination to permit abandonment that New York was compelled to expend monies in an effort to safeguard the public. That initial determination is what the court below properly rejected.[22] New York's right to recover those monies is not at issue in this proceeding, as the court of appeals found. *Quanta*, 739 F.2d at 923 (App. A, 25a).

v. The Trustee's Expenditure of Funds to Prevent Violations of Federal and State Environmental Laws Is a Necessary Cost of Preserving the Estate.

To hold that the trustee cannot abandon the property in violation of federal and state environmental laws is concededly to require the trustee to continue to expend funds to assure compliance with those laws. That, the court of appeals noted, is what Congress intended generally, *i.e.*, to prevent government from assuming all the costs of toxic waste dumping. 739 F.2d at 922 n.10 (App. A, 22a n.10). The issue now before this Court, however, is not whether in a distribution of assets the secured creditors' claims can be subordinated to government's claims for expenditures for a complete cleanup. It is whether the trustee can be compelled to expend estate funds to maintain the property until government or the trustee or both have taken necessary steps to assure that the property can be disposed of in compliance with federal and state environmental, health and safety laws.

The specific authorization for this action by the trustee, we submit, is the provision of 11 U.S.C. § 503(b)(1)(A) (1982) allowing the trustee to pay the "actual, necessary costs of preserving

[22] The issue of the trustee's obligation to clean up the site is not, as he contends (T. Br. 7), moot. First, as the court below found, the cleanup was only partial and the subsoil at the hazardous waste site remains contaminated. *Quanta*, 739 F.2d at 914 (App. A, 6a). Second, even if the cleanup had been completed, the trustee's approach would preclude appellate review of this question of critical public concern whenever the court declined to stay an order of abandonment pending appeal. Under long-settled principles, cases such as this which are "'capable of repetition, yet evading review,'" *Roe v. Wade*, 410 U.S. 113, 125 (1973) (quoting *Southern Pacific Terminal Co. v. Interstate Commerce Commission*, 219 U.S. 498, 515 (1911)), are not moot.

the estate." It does no violence to the language of the Bankruptcy Code to find that maintaining guard service, retaining fire-fighting equipment and patching leaky tanks are necessary costs of preserving the estate until such time as the property can be abandoned or otherwise disposed of lawfully. *Ottenheimer v. Whitaker*, 198 F.2d at 290.

Surely, as a matter of economic preference, secured creditors would wish that the costs of compliance with environmental laws be borne not by their debtor but by the public generally, whether or not the debtor is in bankruptcy. Congress, however, has expressed a different intent. Insuring that private parties with commerical interests at stake do not literally dump their problems on the general public provides the rationale for treating costs of at least maintaining the *status quo* as necessary administrative expenses. *In re T.P. Long Chemical, Inc.*, 45 Bankr. at 286-87; *In re Vermont Real Estate Investment Trust*, 25 Bankr. 804 (Bankr. D. Vt. 1982); *see* L. King, 3 *Collier on Bankruptcy*, ¶503.04 at 503-515 (15th ed. 1983).[23]

Concededly, there may come a point at which requiring the trustee over a lengthy period to exhaust all available assets of the estate to prevent or remedy violations of the law can no longer be characterized as benefiting the dwindling estate. *See In re T.P. Long Chemical, Inc.*, 45 Bankr. at 287-90. That, however, is not the situation posed by New York to the bankruptcy court. Here, and in general, New York was concerned with a short-term necessity: preventing an abandonment that threatened public safety, by having the court direct that the trustee expend whatever funds were necessary to maintain the *status quo* until appropriate corrective measures could be undertaken. That, we have argued,

[23] Although the bankruptcy court reached a different conclusion in *In re Charles George Land Reclamation Trust*, 30 Bankr. 918, 922 n.6 (Bankr. D. Mass. 1983), it ignored the contrary decisions in *Ottenheimer* and *Vermont Real Estate Investment Trust*. The only support cited for its unprecedented decision was the failure of Congress to take any action on a bill introduced before the decisions in *Vermont Real Estate Investment Trust* and *T. P. Long Chemical* which would expressly ratify the *Ottenheimer* interpretation of the Code. Legislative history such as this, however, is entitled to little weight. In any event, the proposed amendment became unnecessary in light of subsequent decisions.

is compelled by section 959(b) and case law delimiting the trustee's power to abandon dangerous property. Requiring the trustee to continue to undertake such administrative expenses was well within the general equitable powers of a bankruptcy court. *See, generally, Pepper v. Litton*, 308 U.S. 295 (1939); *see also Reading Co. v. Brown*, 391 U.S. 471 (1968) (Harlan, J.) (holding, in view of general purposes of administrative expense provision and the Bankruptcy Act as a whole, as well as principles of equity, that tort claims against a receiver under Chapter XI prior to bankruptcy were entitled to status of administrative expenses). At such time as the purposes of the Bankruptcy Code would no longer be served by indefinitely maintaining such a state of affairs, the bankruptcy court could, as an alternative to permitting abandonment, dismiss the Chapter 7 proceedings, as in the case of *In re Charles George Land Reclamation Trust* relied upon by the trustee (T. Br. 18-19),[24] so that a receiver might be appointed by the state courts. *See In re 30 Hill Top Street Corp.*, 42 Bankr. at 522.

C. The Trustee May Not Abandon Property in Violation of State and Local Health, Safety and Environmental Requirements.

We have argued above that this case does not present for decision the issue of whether the abandonment provisions of the Bankruptcy Code preempt state and local environmental laws. However, to the extent New York here was enforcing its own laws as well as parallel federal laws, application of New York's laws was not preempted by section 554(a).

Consideration of whether a state provision violates the supremacy clause "starts with the basic assumption that Congress does not intend to displace state law." *Maryland v. Louisiana*, 451 U.S. 725, 746 (1981).

Here, there is no question of express preemption. Indeed, Congress, we have argued, expressly mandated in 28 U.S.C. § 959(b)

[24] The court there noted that dismissal "would allow the EPA and the [state environmental agency] to assert their full panoply of powers under the Federal and State Superfund statutes." 30 Bankr. at 925.

that there be no preemption of state laws when it directed the trustee to manage and operate the estate consistently with such laws. By simply construing section 959(b) of the Judicial Code and section 362(b)(4) of the Bankruptcy Code as governing section 554(a) of the Bankruptcy Code, we have contended, the Court obviates the need to reach any preemption issue.

The only question remaining is whether requiring the trustee to take elementary steps to protect the public from harm, which are required by state and local laws governing hazardous wastes, would frustrate the purpose of the Bankruptcy Code. *See Maryland v. Louisiana*, 451 U.S. at 746-47 and cases there cited. In New York's view, it clearly would not.

In *Commonwealth Edison Co. v. Montana*, 453 U.S. 609, 633-36 (1981), this Court rejected an effort to suppress a state severance tax because it purportedly frustrated national energy policies established in the Powerplant and Industrial Fuel Use Act of 1978, 42 U.S.C. § 8301(b)(3)(1982). Citing the preemption standards enunciated in *Florida Lime & Avocado Growers, Inc. v. Paul*, 373 U.S. 132, 142 (1963) ("[p]re-emption of state law by federal statute or regulation is not favored 'in the absence of persuasive reasons—either that the nature of the regulated subject matter permits no other conclusion, or that the Congress has unmistakably so ordained'"), this Court rejected the suggestion that "general statements demonstrate a congressional intent to preempt all state legislation that may have an adverse impact. . . ." 453 U.S. at 634, 633. By looking at the energy legislation as a whole, the *Commonwealth Edison* Court found clear indication that the statute contemplated the continued existence of state severance taxes.

Similarly, the Bankruptcy Reform Act of 1978, when viewed as a whole, indicates a clear congressional desire that the state's public health and safety regulations should continue to exist harmoniously with the requirements of the bankruptcy laws. It is difficult to imagine why Congress would direct a trustee to "manage and operate" the estate in compliance with state laws, 28 U.S.C. § 959(b), but yet intend, without so stating, to displace

those same laws under section 554(a) if abandonment were contemplated. Likewise, the court of appeals cited the decision not to stay government enforcement proceedings automatically upon the filing of a bankruptcy petition as additional evidence of Congress' intent not to displace state laws. *Quanta*, 739 F.2d at 918 (App. A, 15a). 11 U.S.C. 362(b)(4) authorizes New York to continue proceedings brought under its "police or regulatory power" notwithstanding the filing of a petition in bankruptcy.[25]

Moreover, by its enactment of TSCA, CERCLA and the Clean Water Act, Congress expressed in no uncertain terms a *national* policy requiring careful, proper disposal of hazardous wastes. Nowhere did it preempt state and local laws directed toward the same end. There is, therefore, every reason to conclude that Congress did not intend to suppress the vital public interest contained in these state and local laws controlling the disposal of hazardous waste when, in the Bankruptcy Reform Act, it provided for the orderly liquidation of a debtor's estate and its expeditious distribution to creditors. Certainly, had such an exception been intended, it could have been written into the Bankruptcy Code's provision on abandonment, section 554(a), or into section 959(b) of the Judicial Code.

[25] In enacting the Bankruptcy Reform Act of 1978, Congress was concerned that bankruptcy courts not use their authority to disrupt the enforcement of statutes adopted pursuant to the states' police power to protect public health and safety and the environment. The House Report makes it clear that the interests of the state in protecting its citizens and its environment are to be carefully balanced against the competing interests of creditors by the Bankruptcy Court:

> Under present law, there has been overuse of the stay in the area of governmental regulation. For example, in one Texas bankruptcy court, the stay was applied to prevent the State of Maine from closing down one of the debtor's plants that was polluting a Maine river in violation of Maine's environmental protection laws. . . . The bill excepts these kinds of actions from the automatic stay. . . . The court will [now] be required to examine the State actions more carefully and with a view to protecting the legitimate interests of the State as well as of the estate. . . .

H.R. Rep. No. 595, 95th Cong., lst Sess. 174-75, *reprinted in* 1978 U.S. Code Cong. & Ad. News 5787, 6135 (footnote omitted).

In *Silkwood v. Kerr-McGee Corp.*, 104 S.Ct. 615 (1984), this Court, in support of its holding that federal law does not preempt state standards for damages due to radiation injuries, observed that there was no indication that Congress ever seriously considered precluding the use of state remedies. This silence was "particularly significant" since it "is difficult to believe that Congress would, without comment, remove all means of judicial recourse for those injured by illegal conduct." 104 S.Ct. at 623. Similarly, given the silence that accompanied the enactment of section 554(a), it is difficult to believe that Congress intended, without comment, to work so drastic a change of previously developed judicial doctrine and recently enacted statutes as to permit a trustee to disregard public health, safety and environmental laws. Applying the reasoning of such cases as *Commonwealth Edison Co. v. Montana* and *Silkwood v. Kerr-McGee*, the court below properly refused to infer "such a radical change in the nature of local public health and safety regulations—the substitution of governmental action for citizen compliance without an indication that Congress so intended." *Quanta*, 739 F.2d at 921-22 (App. A, 22a).

The trustee contends nonetheless that the supremacy clause requires the suspension of the states' public health and hazardous waste laws as to him because operation of these state laws frustrates the purpose of the Bankruptcy Code. (T. Br. 17.) The preceding discussion, however, demonstrates that federal laws themselves seek to assure that valid governmental regulations are obeyed during the orderly liquidation of assets and their distribution to creditors. Congress, therefore, has determined that bankruptcy policy is not by its nature antagonistic to or irreconcilable with public health and safety laws, nor is there an "impossibility of dual compliance," *Florida Lime & Avocado Growers v. Paul*, 373 U.S. at 143. Certainly the courts have not viewed these statutory schemes as mutually exclusive. Cases such as *Ottenheimer v. Whitaker* and *Lewis Jones*, taken together with the directives of 28 U.S.C. § 959(b) and 11 U.S.C. § 362(b)(4), make clear that the trustee's power under the bankruptcy laws and the public health and safety concerns expressed in state law not only can be reconciled but, in Congress' view, must be reconciled.

Thus, it cannot be said that state and local environmental law "stands as an obstacle to the accomplishment and execution of the full purposes and objectives of Congress," *Hines v. Davidowitz*, 312 U.S. 52, 67 (1941), where Congress itself has required what New York also demands: the safe, proper disposal of hazardous substances.

II. LIMITING THE TRUSTEE'S POWER TO ABANDON PROPERTY IN VIOLATION OF FEDERAL AND STATE ENVIRONMENTAL LAWS IS NOT A "TAKING" UNDER THE FIFTH AMENDMENT.

The court below correctly determined, based on a long line of decisions by this Court, that state enforcement of environmental laws, even when it causes financial expenditure or economic loss, is not a "taking" under the fifth amendment. *Quanta*, 739 F.2d at 922 n.11 (App. A, 23a n.11). Nevertheless, the trustee claims that limiting his power to abandon pursuant to section 554(a) is inconsistent with this Court's decision in *United States v. Security Industrial Bank*, 459 U.S. 70 (1982), and violates the takings clause of the fifth amendment. (T. Br. 20-22).[26] As demonstrated below, these contentions lack merit for at least three reasons. First, the issue is not ripe. Second, as this Court has long recognized, a state's enforcement of its environmental laws is not a "taking" even if it results in total destruction of the value of the property. Third, neither *Security Industrial Bank* nor any of the limited exceptions to this long-settled rule is applicable here.

A. The Fifth Amendment Takings Issue Is Not Ripe for Adjudication by this Court.

The court below did not reach the question of what, if any, estate funds should now be devoted to reimbursing New York for the Quanta cleanup, but rather remanded that question to the bankruptcy court to make appropriate findings of fact. *Quanta*, 739 F.2d at 923 (App. A, 25a). The bankruptcy court has made no findings of fact as to what assets are available, to what extent claims are secured or unsecured, what types of secured claims exist, how the secured claims were created and what were the secured creditors' reasonable expectations. It is, therefore, premature for this Court to examine that question at this stage of the proceedings since "there is as yet no concrete controversy regarding the application" of the court of appeals decision. *Agins v. City of Tiburon*, 447 U.S. 255, 260 (1979).

[26] The petitioner in the companion case, *Midlantic National Bank v. New Jersey Department of Environmental Protection*, No. 84-801, advances the same argument. (Midlantic Br. 11-16).

This conclusion is particularly compelling in the present context because this Court has often observed that no "set formula" has been developed "for determining when justice and fairness require that economic injuries caused by public action must be deemed a compensable taking," and therefore "the inquiry into whether a taking has occurred is essentially an 'ad hoc, factual' inquiry." *Ruckelshaus v. Monsanto Co.*, 104 S. Ct. at 2874, citing *Kaiser Aetna v. United States*, 444 U.S. 164, 175 (1979).

B. Valid Government Regulations which Cause Significant Economic Loss Do Not Violate the "Takings Clause" of the Fifth Amendment.

This Court has consistently rejected challenges to legitimate government regulations under the takings clause, even where compliance would result in the complete destruction of the value of the company's property. Moreover, this Court has done so in cases that by no stretch of the imagination involve the potentially catastrophic consequences to public health and safety involved here.

In *Ruckelshaus v. Monsanto*, the manufacturer of pesticides argued that federal regulations that could result in the public disclosure of trade secrets, thus completely destroying the value of the company's property, violated the takings clause of the fifth amendment. This Court rejected Monsanto's argument and declared that the burdens of government regulation were particularly justified in the sale and use of pesticides, which had long been the subject of public concern and governmental regulation. The economic burdens that accompany government regulation are the price we pay for "the advantage of living and doing business in a civilized community." 104 S. Ct. at 2875 (quoting *Pennsylvania Coal Co. v. Mahon*, 260 U.S. 393, 422 (1922) (Brandeis, J., dissenting)).

Similarly, in *Goldblatt v. Hempstead*, 369 U.S. 590 (1962), this Court upheld a local safety ordinance which prohibited a sand and gravel company from excavating below the water table, a level it had previously reached. This Court did so even though

compliance with the ordinance would result in a complete prohibition of the beneficial use to which the property had been devoted for the preceding thirty-five years and meant the total destruction of the business enterprise. In rejecting the company's "takings clause" argument, this Court quoted *Mugler v. Kansas*, 123 U.S. 623, 669 (1887), as authority for the proposition that

> [t]he power which the States have of prohibiting such use by individuals of their property as will be prejudicial to the health, the morals, or the safety of the public, is not – and, consistently with the existence and safety of organized society, cannot be – burdened with the condition that the State must compensate such individual owners for pecuniary losses they may sustain, by reason of their not being permitted, by a noxious use of their property, to inflict injury upon the community.

Goldblatt, 369 U.S. at 593.[27]

The trustee's suggestion that requiring the estate to comply with federal and state public health and environmental laws would violate the takings clause with respect to the creditors' property interest in the estate does not withstand scrutiny. Contrary to the trustee's contention, compliance with the federal and state regulations which are at issue here does not necessarily extinguish any property right held by the creditors. Under the ruling of the court below, unsecured creditors (who of course have no protected interest in the estate) can still look to the general assets remaining in an estate and secured creditors can still look to specific property that secures their claim. Therefore, this case is unlike *United States v. Security Industrial Bank*, where the very lienhold interest would have been retroactively extinguished.

[27] This Court has routinely rejected similar challenges to generally applicable state regulation which caused expenditure of funds or severe economic loss. *See, e.g.*, *Agins v. City of Tiburon* (municipal zoning ordinances restricting the type and density of buildings held not a taking); *Penn Central Transportation Co. v. New York City*, 438 U.S. 104 (1978) (landmark preservation ordinance); *Village of Euclid v. Ambler Realty Co.*, 272 U.S. 365 (1926) (industrial zoning regulation); *Hadacheck v. Sebastian*, 239 U.S. 394 (1915) (municipal ordinance prohibiting brickmaking).

The creditors' real concern in this matter is not with the issue of compliance with legitimate government regulations *per se*, or with the actual extinguishing of a property right; rather, they are concerned, in practical terms, that after compliance with the law there will be significantly less value in the general assets of the estate and less value in the secured property, possibly none at all, to satisfy their claims.[28] Creditors, however, advance funds with the hope of a profitable return but with full knowledge that the business enterprise they are underwriting may fail for any one of a number of reasons, including the cost of their debtor's compliance with public health and environmental regulations. *See also In re T.P. Long Chemical Inc.*, 45 Bankr. at 287 ("Creditors must generally bear the risks of any enterprise."). That is the risk that every creditor voluntarily undertakes in extending credit, *i.e.*, that its debtor may need to expend *some* of its resources to obey laws governing its business. Any creditor of a business such as Quanta's assuredly had a "reasonable investment-backed expectation," *Ruckelshaus v. Monsanto Co.*, 104 S. Ct. at 2875, that Quanta might need to spend money to comply with generally applicable environmental laws in effect at the time of the borrowing which plainly regulated the very essence of Quanta's business.

What the court below held, in effect, was that the creditors' security interests simply do not require the public to underwrite the risks those creditors knew of and must have assumed. In other words, government is not obligated to expend public funds to

[28] It is well established that unsecured creditors may only look to the unencumbered assets of the estate, if there are any, to satisfy their claims. *See Hanover National Bank v. Moyses*, 186 U.S. 181 (1902). Without the benefit of factual findings it is more difficult to address the issue of secured creditors. The status of Midlantic National Bank, the petitioner in the companion case, *Midlantic National Bank v. New Jersey*, No. 84-801, is illustrative. Although Midlantic asserts the status of a secured creditor, its secured interest does not reside in any definable piece of property but rather consists of the debtor's "inventory," *i.e.*, salable waste oil to the extent that any exists and in "accounts receivable" to the extent that such accounts may exist. *See* Midlantic Br. 6-7. Compliance with government regulations does not destroy Midlantic's rights as a secured creditor. It only diminishes the value of that property.

meet the regulatory obligations of private parties (here, the estate and the trustee in his representative capacity) in order to cushion the creditors' foreseeable risk on their investments. That, in general terms, parallels the very conclusion Congress reached in enacting numerous environmental laws during the past decade.

C. Neither *United States v. Security Industrial Bank* nor the "Erosion Taking" Doctrine Permits Abandonment Here.

As demonstrated above, state enforcement of federal and state environmental laws, even when it causes the complete destruction of the value of the property, is not a "taking" under the fifth amendment. Neither *United States v. Security Industrial Bank* nor the "erosion taking" doctrine alters this conclusion.

In *Security Industrial Bank*, this Court considered a challenge under the takings clause to the retrospective application of section 522(f)(2) of the Bankruptcy Code to invalidate liens acquired before the effective date of the Bankruptcy Reform Act of 1978. It held that when there is "substantial doubt whether the retroactive destruction of the appellees' liens in this case comports with the Fifth Amendment," 459 U.S. at 78, it would consider as a matter of statutory construction whether section 522(f)(2) must necessarily be applied in that manner. *Id.* It considered the statutory question first under the basic principle set forth in *Crowell v. Benson*, 285 U.S. 22, 62 (1932), that "this Court will first ascertain whether a construction of the statute is fairly possible by which the constitutional question may be avoided."

Here, however, the trustee has failed to demonstrate "substantial doubt" that enforcement of federal and state environmental laws raises a taking question. The *only* cases cited by the trustee or the dissent in the court below in support of their contention that limiting the power of the trustee to manage or abandon the property where it would harm the public interest are the "erosion taking" cases. (T. Br. 21 n.5); *Quanta*, 739 F.2d at 924-26 (Gibbons, J., dissenting) (App. A, 28a-32a). As the court below recognized, however, this doctrine is limited to railroad reorganization cases and requires a balancing of losses to the estate

against the public interest. *Quanta*, 739 F.2d at 922 n.11 (App. A, 23a n.11). The trustee has failed to show that any potential losses to the estate necessitated by protecting the public from leaking chemicals and possible fires would cause "losses unreasonable even in light of the public interest." *Regional Railroad Reorganization Act Cases*, 419 U.S. 102, 124 (1974).

CONCLUSION

For all the foregoing reasons, this Court should affirm the order of the Court of Appeals for the Third Circuit.

Dated: June 7, 1985
New York, New York

Respectfully submitted,
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Nos. 84-801 and 84-805

In the Supreme Court of the United States

OCTOBER TERM, 1985

MIDLANTIC NATIONAL BANK, PETITIONER

v.

NEW JERSEY DEPARTMENT OF
ENVIRONMENTAL RESOURCES

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

THOMAS J. O'NEILL, PETITIONER

v.

CITY OF NEW YORK

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

MOTION FOR LEAVE TO FILE AND BRIEF FOR *AMICUS CURIAE*

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39 pp

IN THE SUPREME COURT OF THE UNITED STATES

October Term, 1985

No. 84-801

MIDLANTIC NATIONAL BANK, Petitioner

v.

NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION

No. 84-805

THOMAS J. O'NEILL, Petitioner

v.

CITY OF NEW YORK

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF *AMICUS CURIAE*

Pursuant to Rule 36.3, the undersigned, who is contemporaneously applying for admission to the Bar of this Court, and who is appearing *pro se*, moves for leave to file the attached brief as an *amicus curiae* in the

event that consent to the filing of the brief is not granted by all the parties.

The *amicus* is a teacher and scholar of the bankruptcy law. The issues in this case involve a subject in which he has a special interest and about which he has written. Except for that academic interest, he has no interest in the outcome of this case.

Amicus believes that he takes a view of the issues involved in this case and their proper resolution that is distinct from that likely to be taken by any of the parties. The issues are important, and in resolving them the Court should have the benefit of a presentation of all the competing views. *Amicus* believes that in submitting this brief, he is acting within the core meaning of a brief *amicus curiae*.

CONCLUSION

For the reasons stated, the motion for leave to file the attached brief should be granted.

Respectfully submitted.

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April, 1985

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ENVIRONMENTAL PROTECTION

THOMAS J. O'NEILL, Petitioner

v.

CITY OF NEW YORK

BRIEF FOR AMICUS CURIAE

SUMMARY OF ARGUMENT AND INTRODUCTION

Quanta Resources Corp. ("Quanta") owned and operated a waste oil storage and processing facility in New York City.[1] The

1. The facts describe No. 84-805, Thomas J. O'Neill v. City of New York. A companion case, No. 84-801, Midlantic Nat'l Bank v. New Jersey Dept. of Envtl. Protection, involves an indentical issue concerning the abandonment of a waste oil and oil sludge site in

site on which it was located contained storage tanks with hundreds of thousands of gallons of waste oil and other chemicals. Approximately 70,000 of these gallons were contaminated with polychlorinated biphenyls ("PCBs"). Quanta filed a voluntary petition in bankruptcy under Chapter 11 of the Bankruptcy Code, 11 U.S.C. § 301, on October 6, 1981. The bankruptcy case was converted to Chapter 7, the liquidation chapter, a little over a month later, on November 12, 1981.

Bringing the waste oil storage site into compliance with a variety of federal, state, and local laws governing the storage and disposal of PCBs would have required a substantial expenditure of funds. The trustee in bankruptcy concluded

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Edgewater, New Jersey. The New Jersey Department of Environmental Protection, however, has not asserted that it should be reimbursed for clean-up expenses, In re Quanta Resources Corp., 739 F.2d 927, 929 (3d Cir. 1984). For that reason, Amicus will concentrate on the case involving the City of New York.

that the expenditures that would be required to bring the site into compliance with those environmental statutes would have exceeded the value of the property, rendering the site a net burden to the estate. The trustee thereupon moved to abandon the property pursuant to Section 554 of the Bankruptcy Code, 11 U.S.C. § 554. The City of New York (the "City") objected to that action, on the ground that abandonment of the property would constitute a disposal of the hazardous wastes, in violation of state and local law. In addition, the City asserted that abandonment of the site would create a continuing violation of state and local hazardous waste storage laws.

The bankruptcy court permitted the abandonment over the objections of the City and refused to stay its order pending appeal. As a consequence, the property was abandoned and the City thereupon proceeded to clean up the site, with the exception of the

contaminated subsoil.[2] This clean up cost the City approximately $2.5 million. The City had sought, and the bankruptcy judge had refused to grant the City, a first lien on the property to the extent of such expenditures.

The City appealed the order to the district court, without raising the question of its right to a lien on the site. The district court affirmed the order on January 24, 1983. The City thereupon appealed to the Third Circuit Court of Appeals which, on July 20, 1984, reversed the judgment, one judge dissenting. In re Quanta Resources Corp., 739 F.2d 912 (3d Cir. 1984).[3] The Third Circuit viewed the issue to be resolved as one of "balancing"

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2. The property was subject to two mortgages. Apparently because the site was without value while subject to the clean-up requirement, the mortgagees abandoned their mortgages on the property. See 739 F.2d., at 914 n.3.

3. The companion case, No. 84-801, involving the New Jersey Department of Environmental Protection, was reversed on the basis of that opinion, In re Quanta Resources Corp., 739 F.2d 927 (3d Cir. 1984).

environmental policies with bankruptcy policies, as reflected in the provision permitting abandonment. It viewed the balance as landing on the side of the environmental laws, reasoning, 739 F.2d, at 921-22:

> But the extent . . . of the expenditures necessary to dispose of the waste properly is not in itself sufficient to outweigh the public interest at stake here. . . . If trustees in bankruptcy are to be permitted to dispose of hazardous wastes under the cloak of the abandonment power, compliance with environmental protection laws will be transformed into governmental cleanup by default. It cannot be said that the bankruptcy laws were intended to work such a radical change in the nature of local public health and safety regulation — the substitution of governmental action for citizen compliance -- without an indication that Congress so intended. The supremacy clause does not require the suspension of the operation of New York's hazardous waste disposal laws.

The Third Circuit, however, did not reach the issue of the priority, if any, on Quanta's remaining assets of the claim of the City for the clean up, finding that to be an issue "that can properly be resolved only by the bankruptcy court," 739 F.2d, at 923.

This Court granted certiorari on

February 19, 1985.

The Third Circuit's approach to this problem is wrong.[4] The Third Circuit went astray by perceiving there to be a conflict between bankruptcy law and environmental law. Proper analysis of the question reveals that no such conflict exists. Bankruptcy law is primarily a procedural forum for collecting

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4. Amicus suggests, however, that this Court may want to consider dismissing these cases, on the ground that certiorari was improvidently granted. On the issue of the propriety of abandonment, the Third Circuit's answer, although wrong in amicus' view, is actually dicta. The property was abandoned; no stay was obtained. The City has cleaned up the site itself. It would therefore appear that the only remaining issue in No. 84-805 is whether the City can get repaid for its expenses in cleaning up the site. No holding on that issue is before this Court. The City did not appeal the bankruptcy judge's determination that it did not have a first lien on the abandoned property, nor is there any ruling as to who now owns the site. No lower court has yet ruled on the issue of the priority of the claim of the City against Quanta's remaining assets. Indeed, the Third Circuit expressly remanded for consideration of that issue, 739 F.2d, at 923. The posture of the companion case seems substantially similar, 739 F.2d, at 929.

The remainder of this brief will assume, contrary to that point, that the Court does not dismiss these cases on the ground that certiorari was improvidently granted.

assets and distributing them to claimants according to their nonbankruptcy entitlements. The real issue in this case, as Judge Gibbons noted in dissent, 739 F.2d, at 923, is not one of weighing the relative importance of a bankruptcy policy in favor of abandonment, but, rather, one of deciding what is the priority of various claims against the assets that do exist. Resolution of that question, however, is determined by nonbankruptcy law. It is simply wrong to view bankruptcy policy as somehow affecting the answer to this problem.

The proper analysis would be to ask what would have happened had Quanta dissolved under state law without ever passing through bankruptcy. If Quanta is insolvent, it will not be able to pay in full all those with claims against it. That is a fact that is not a matter of bankruptcy law, but rather of the reality of too few assets (a problem created, in part, by long established state

law rules regarding limited liability of shareholders for the debts of their corporations).[5] In paying off claimants, moreover, some claimants may do better than others. Those with security interests or statutory liens, for example, may be paid in full while general unsecured creditors will share only in what is left over. How well the City would have done in a dissolution of Quanta under state law depends entirely on the status of clean-up obligations under state and nonbankruptcy federal law. The question, ultimately, is: Who pays for the clean-up? To say that the City has first right to all of Quanta's assets is to say that the other creditors must pay for the clean up, at least to the extent of the

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5.. This is not to say that a state could not have a different policy regarding toxic wastes. It could hold managers or principal shareholders personally liable. It could require bonding or insurance by any firm dealing in toxic wastes. None of these responses, however, is involved in the current cases.

value of those assets. To say that the City does not have first right, means that the City will share with the other general creditors in Quanta's limited assets in a dissolution of Quanta under state law. To the extent its claim is unsatisfied in that distribution, the City will have to bear the cost itself. But that result cannot involve bankruptcy policy, because bankruptcy is not involved at all when a corporation dissolves under state law.

Nothing changes -- or should change -- in bankruptcy. The question of abandonment in this case has obscured the only important issue -- which is the one the Third Circuit did not decide. The City may have priority over the other creditors of Quanta with respect to its claim based on the money spent to clean up the waste site. But if it does, that is because nonbankruptcy law gives it that priority, and would recognize that priority in a dissolution of Quanta under

state law. No bankruptcy policy is involved; there is no bankruptcy policy to "balance" with environmental policy. Refusing to permit abandonment is tantamount to saying that all of Quanta's assets must be devoted first to cleaning up the site. But all that does is to resolve an identical priority issue by favoring the claim based on a clean-up right over the claims of other creditors of Quanta. No court has examined whether that is the proper resolution of the priority issue as a matter of nonbankruptcy law, and bankruptcy law takes -- and should take -- property (and priority) rights as they are established by nonbankruptcy law. To hold abandonment is improper obscures the real issue in this case, and may change relative nonbankruptcy entitlements, encouraging the kind of "forum shopping" denounced by Butner v. United States, 440 U.S. 48, 54-55 (1979).

ARGUMENT

Before running to bankruptcy policy, it is useful to understand what would have happened had no bankruptcy petition been filed. When that is done, it is clear that the core issue in this case concerns not a conflict with bankruptcy policy but the fact of a corporation that is insolvent and cannot pay all its debts in full. Because of that fact, one must face the question of who gets the assets that are there in what order -- a question of priority among claimants. In particular, the underlying question is the status of the City's claim based on either its right to have the site cleaned up or its right to be reimbursed for cleaning up the site itself. Resolution of this issue involves considering the general effects of state, and perhaps federal, law. But to focus on bankruptcy policy, and specifically on abandonment, as somehow at the crux of

this dispute is, as amicus will show, a red herring.[6] Indeed, it is worse: disallowing

6. The Third Circuit relied, in part, on the impact of § 362(b)(4), 11 U.S.C. § 362(b)(4), excepting from the automatic stay state actions to protect the health and safety of the public. Relying on Penn Terra Ltd. v. Department of Envtl. Resources, 733 F.2d 267 (3d Cir. 1984), the Third Circuit in this case viewed the clean-up order as exempt from the automatic stay. This approach suffers from exactly the same infirmities as does the Third Circuit's abandonment analysis; indeed, the core issue in the two cases is identical. Section 362(b)(4) has a natural reading. The automatic stay should not apply to governmental regulations that tell a firm not to pollute in the future. That is a cost of doing business, and the fact that a bankruptcy proceeding has commenced should be irrelevant. Section 362(b)(4) makes it irrelevant: the automatic stay will not protect a debtor in bankruptcy from ongoing regulatory orders (such as if debtor emits pollutants in its operations, it must install a scrubber to continue to operate). But that cannot apply to this case. Quanta is liquidating. It has no future business. The issue in this case is who pays for the clean-up of something Quanta did in the past. As such, it is a "claim" based on a pre-bankruptcy action of Quanta. Ohio v. Kovacs, 105 S.Ct. 705 (1985). The automatic stay should apply (at least in the first instance); if it did not, and Quanta had to do the clean up, one again would be resolving, without even confronting, the underlying issue of priority. If the claim is an unsecured claim, the stay should not be lifted. This does not mean that the clean up should not take place. Nothing in § 362(b)(4) should prohibit the governmental unit from effecting the clean-up itself. It is simply a question, again, of who pays for it. See Baird & Jackson, Kovacs and Toxic Wastes in Bankruptcy, 36 Stan. L. Rev. 1199, 1199 n.3, 1202-10 (1984).

abandonment, to the extent it is tantamount to requiring the trustee to effect a clean up, resolves an underlying priority issue whose answer should be given by nonbankruptcy law. See 739 F.2d, at 923 (Gibbons, J., dissenting); see generally Jackson, Translating Assets and Liabilities to the Bankruptcy Forum, 15 J. Legal Studies 73 (1985).

The question in this case is not whether Quanta must comply with the environmental laws of New York with respect to future operations. If it had wanted to continue in business, it, like any other business, would have had to comply with those environmental laws or pay the penalty. Cf. Reading Co. v. Brown, 391 U.S. 471 (1968) (post-bankruptcy tort a cost of doing business entitled to priority over pre-bankruptcy claimants). If those laws prohibited it from dumping PCBs at its site, it would not -- and should not -- be permitted to dump PCBs in the future. But

that cannot be the issue in this case. Quanta is liquidating. Quanta will have no future operations. At issue in this case is who pays for the clean up of a pre-bankruptcy violation of environmental laws. To say that Quanta must pay is to say that Quanta's creditors must pay, because Quanta is insolvent.[7] The holding of the Third Circuit prohibiting abandonment apparently means that the trustee must use all of Quanta's assets to clean up the site. But that is tantamount to a holding that the claim of the City based on that clean-up right[8] has priority over all the other creditors of Quanta. That holding, however, implicates state (and perhaps federal) law policy. It is not a bankruptcy

7. If Quanta is not insolvent, then all its claimants — including the City -- will be paid in full and there is no issue worth litigating.

8. As to why a clean up right is a "claim," see Ohio v. Kovacs, 105 S.Ct. 705 (1985); Baird & Jackson, Kovacs and Toxic Wastes in Bankruptcy, 36 Stan. L. Rev. 1199 (1984).

issue. Indeed, the Third Circuit, when it faced the issue directly, refused to resolve it.[9] Focusing on abandonment misses what is at issue.

This case, although it ostensibly involves a different section of the Bankruptcy Code, is remarkably similar to Ohio v. Kovacs, 105 S.Ct. 705 (1985). In Kovacs, the focus was on whether a clean up obligation was a "claim" or a "debt" under 11 U.S.C. §§ 101(4) and (11). But by initially resorting to those sections, the litigants obscured the real issue. In Kovacs, as in this case, the real question was not whether something was a claim (it was) or whether the trustee can abandon property (he can) but rather a question of priority among

9. This odd result is a consequence of the fact that the "no abandonment" decision in this case was actually dicta. Abandonment had occurred and the City had already cleaned up the site. See note 4 supra (discussing whether this case should be dismissed on the ground that certiorari was improvidently granted).

claimants. Resolution of that issue raises, in different garb, the analysis used by this Court in Chicago Board of Trade v. Johnson, 264 U.S. 1 (1924). And that question is whether the City has a property right, equivalent to a statutory lien or a security interest, in Quanta's assets to secure performance of that obligation.

Not all claims are created equal by state law, and bankruptcy law, which is largely procedural, generally respects the different attributes of state-law claims.[10] For that reason, a longstanding policy of bankruptcy law is that it respects the value

10. This respect is not accorded to state laws that have an effect only in bankruptcy — state-created priorities and spurious statutory liens, 11 U.S.C. § 545. But if the property interest (whether labeled a lien or not), although created by statute, is effective against competing claimants in and out of bankruptcy, no provision of the Bankruptcy Code and no bankruptcy policy invalidates the interest. See In re Anchorage International Inn, Inc., 718 F.2d 1446 (9th Cir. 1983); In re Telemart Enterprises, Inc., 524 F.2d 761 (9th Cir. 1975); Jackson, Bankruptcy, Non-Bankruptcy Entitlements, and the Creditors' Bargain, 91 Yale L.J. 857, 901-06 (1982).

of property rights created by state law to the extent that doing so is not inconsistent with the goals of the bankruptcy process. As this Court noted in Butner v. United States, 440 U.S. 48, 54-55 (1979):

> Property interests are created and defined by state law. Unless some federal interest requires a different result, there is no reason why such interests should be analyzed differently simply because an interested party is involved in a bankruptcy proceeding. Uniform treatment of property interests by both state and federal courts within a State serves to reduce uncertainty, to discourage forum shopping, and to prevent a party from receiving "a windfall merely by reason of the happenstance of bankruptcy." Lewis v. Manufacturers National Bank, 364 U.S. 603, 609.

For example, if a claim is secured, or the subject of a statutory lien or a statutory trust, the claim is entitled to be paid first out of the associated assets, 11 U.S.C. § 725. See also Ohio v. Kovacs, 105 S.Ct. 705, 712 (1985) (O'Connor, J., concurring).[11]

11. Equally, if such a claim is not paid in bankruptcy, the "lien" given by statute or the secured contract will "pass through" bankruptcy and be enforceable against the debtor's pre-bankruptcy property, notwithstanding that the underlying debt

The real question in this case is the status of the rights of the City against the property of the estate created by 11 U.S.C. § 541. And that, in turn, involves a question of the relative "priority"[12] of the right the City has to use those assets to satisfy its claim vis-a-vis the rights of holders of other pre-petition obligations. This priority can result not only from consensual security interests, statutory liens, or statutory trusts -- all cases of which are, or should be, uncontroversial -- but also from simply observing the entitlements of a

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itself was discharged. This doctrine, which was first enunciated by this Court in Long v. Bullard, 117 U.S. 617 (1886), continues in the current Bankruptcy Code. Section 524(a)(2), 11 U.S.C. § 524(a)(2); see H. Rep. No. 595, 95th Cong., 1st Sess. 361 (1977) ("[t]he bankruptcy discharge will not prevent enforcement of valid liens. The rule of Long v. Bullard . . . is accepted with respect to the enforcement of valid liens on nonexempt property as well as on exempt property.").

12. The word is being used here in its generic sense, not in its specific bankruptcy sense, where it refers only to priority among unsecured creditors, 11 U.S.C. § 507.

particular claimant under state law to the asset vis-a-vis others. The priority right of a particular claimant, in other words, may be inherent in the restrictions placed by the state on the use of property in the first instance.[13]

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13. The classic case illustrating this feature of how bankruptcy law must be sensitive to state attributes in evaluating rights among claimants, and not to state (or bankruptcy) labels, is Chicago Board of Trade v. Johnson, 264 U.S. 1 (1924). That case involved a question of how to treat membership by the bankrupt in the Chicago Board of Trade. The District Court and the Seventh Circuit had concluded that the membership was "property" and passed to the trustee in bankruptcy free of all claims of the members and, accordingly, could be sold for the benefit of the general creditors. This Court reversed. Because of rules of membership on the Chicago Board of Trade, a member could not sell his membership, over the objection of another member, unless and until all debts owed by the member to other members were paid in full. Even though the other members did not enjoy the right "to compel sale or other disposition of memberships to pay debts," this Court did "not think this makes a real difference in the character of the property which the member has in his seat." 264 U.S., at 11. The "property" involved — the membership — was defined so as to carry with it a limitation on its value to the bankrupt (and his general creditors): debts to other members had to be satisfied before value could be derived from the membership that benefitted the remaining claimants. Noting that this right was "in some respects similar to the typical lien of the common law," id., this Court held that "[t]he lien, if

It is the resolution of this priority issue -- an issue to which bankruptcy policy is unconcerned -- that is at the core of this case. But in order to see why it, and not the issue of abandonment, is the proper focus, it is worth first considering the case of a debtor that is a corporation and three

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it can be called such, is inherent in the property in its creation, and it can be asserted at any time before actual transfer . . . ." Id., at 15. For that reason, this Court reversed the Seventh Circuit and held that "[t]he claims of the petitioners [members on the Chicago Board of Trade] . . . must be satisfied before the trustee can realize anything on the transfer of the seat for the general estate." Id.

The principle announced in Chicago Board of Trade is a fixed feature of bankruptcy law, and is fully consistent with the admonition in Butner v. United States, 440 U.S. 48, 54-55 (1979), that property rights are created and defined by state law and should be followed in bankruptcy unless the bankruptcy statute clearly directs otherwise. See, e.g., In re Anchorage International Inn, Inc., 718 F.2d 1446 (9th Cir. 1983) (provision of state statute requiring liquor-related debts to be paid before transfer of liquor license would be approved, was tantamount to a "lien" in the license, and would be recognized in bankruptcy). It is the principle that Justice O'Connor recognized in concurring in Ohio v. Kovacs, 105 S.Ct. 705, 712 (1985). See Baird & Jackson, Kovacs and Toxic Wastes in Bankruptcy, 36 Stan. L. Rev. 1199 (1984).

different cases: a case where the debt in question is treated entirely like an unsecured claim; a case in which it is treated as tantamount to having a statutory lien or security interest in the affected asset; and, finally, a case where the obligation in question is effectively secured by all of the corporation's assets.

CASE 1: UNSECURED OBLIGATION

> Debtor has assets (other than a dump site) worth $450,000, $900,000 of unsecured obligations, and no secured obligations. In addition, Debtor is obligated to State to clean up a PCB dump site. Clean-up will cost $100,000. Once cleaned up, the dump site will be worth $50,000.

In Case 1, if Debtor were to dissolve under the laws of State, and assuming that State law treated the obligation to State as an unsecured obligation that would not travel with the site property or any of Debtor's other assets, Debtor's assets would be sold for $500,000 and each of the creditors, including State, would receive 50 cents on the dollar. At the conclusion of this

process, there would be no remaining assets or liabilities, and Debtor would dissolve. Unless the sale of the assets involved a fraudulent conveyance or the like, the purchasers would also take the assets free of any liabilities of Debtor, including (under the assumptions of Case 1) the obligation to State.

Nothing really changes -- or should change -- if Debtor is to file a Chapter 7 proceeding in bankruptcy. In that case, the sale of assets and distribution of proceeds is accomplished in bankruptcy, and the claimants all get 50 cents on the dollar, 11 U.S.C. § 726. No discharge is given, 11 U.S.C. § 727(a)(1). But this is not a substantive change. Debtor is free now to dissolve under State law. When Debtor does so dissolve, the claims are, as before, effectively "discharged," because again there would be no Debtor to sue and no assets to go against.

CASE 2: SECURED BY SITE

> **Debtor has assets (other than a dump site) worth \$450,000, and \$900,000 of unsecured obligations. In addition, Debtor is obligated to State to clean-up a PCB dump site. Clean-up will cost \$100,000. Once cleaned up, the dump site will be worth \$50,000. Under applicable law, any owner of the site will be required to clean it up.**

In Case 2, if Debtor were to dissolve under state law, it would sell all its assets other than the dump site. No one would pay anything for the site, because its "clean" value of \$50,000 is swamped by the associated \$100,000 obligation. Unless applicable law provided for shareholder liability, Debtor would dissolve without cleaning up the site. It might thereupon revert to State.[14] When State cleaned up the site, it would have an asset worth \$50,000. Its remaining \$50,000 claim would share pro rata with the other \$900,000 of claimants in the \$450,000

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14. If the State refused to permit dissolution, the corporate shell would continue the nominal owner of this asset. But it would have no assets to use to effect clean-up.

of assets. Again, nothing should change if Debtor is in Chapter 7. Whether labeled "abandonment" or "disposition," State would end up with the site, which would compensate it for half the clean-up cost. State's remaining claim would share in the assets as a general creditor.

CASE 3: SECURED BY ALL ASSETS

> Debtor has assets (other than a dump site) worth $450,000, and $900,000 of unsecured obligations. In addition, Debtor is obligated to State to clean up a PCB dump site. Clean-up will cost $100,000. Once cleaned up, the dump site will be worth $50,000. Due to a state statute, judgments obtained by State for environmental infractions automatically receive a statutory lien on all assets of the infractor and this lien is treated, for all purposes (other than filing) as a security interest under State law.

In Case 3, if Debtor were to dissolve under the laws of State, the assets, if they could be sold free of State's interest, would be sold for $500,000. Unlike before, however, State would be entitled to receive $100,000 first, on account of its statutory lien, and the other creditors would share in the remaining $400,000 of assets pro rata among

their $900,000 of unsecured claims. As before, at the conclusion of this process, Debtor would dissolve. Since State was paid in full, it would have no remaining claim to pursue into the hands of the buyers of the assets.[15] And the unsecured creditors, although not paid in full, have, as before, no one to pursue. Their claims are effectively discharged, as before.

Again, as before, there would be no change if all this occurred in bankruptcy. In a liquidation under Chapter 7, 11 U.S.C. § 725 would require that State, as a secured creditor, be satisfied in full first.[16]

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15. The assets could be sold along with the clean-up liability. In that event, sale of the assets would fetch $400,000. State would pursue its claim against the assets. There is no functional difference.

16. If, for some reason (such as that State never filed a claim in Debtor's bankruptcy proceeding), State's debt would nonetheless be treated the same as it would appear under nonbankruptcy law. In a Chapter 7 proceeding, State would receive nothing (since it did not file a claim), but the purchaser of Debtor's assets would continue to be subject to the obligation to State, see U.C.C. § 9-306(2) (1978). For that

Nothing changes when the issue is one of abandonment of an asset in bankruptcy. Had the trustee not abandoned the property, the question of priority would have to be faced directly. The City might or might not have the equivalent of a statutory lien on the site (Case 2). It also might or might not have the equivalent of a statutory lien on the remaining property of Quanta (Case 3). No court has yet addressed that issue, yet it is the central issue in this case. Abandonment does not change anything. One still needs to face the question of whether nonbankruptcy law treats the relative priority like Case 1, Case 2, or Case 3 (or, indeed, some other outcome). Once that

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reason, a purchaser would paid only $400,000 for the assets, and State could eventually collect the $100,000 owed it out of those assets. See note 15 supra. But it could not sue Debtor once Debtor dissolved under State law, since Debtor ceases to exist as a legal entity. The effect of this is that State can pursue its collateral, but not Debtor. 11 U.S.C. § 524; Long v. Bullard, 117 U.S. 617 (1886).

outcome were determined, bankruptcy policy would call for its value to be respected. Butner v. United States, 440 U.S. 48, 54-55 (1979). By abandoning the site, the trustee has made a determination that the value of the property, cleaned up, is worth less than it would cost to clean it up. Yet that determination does not affect the question of priority. Upon abandonment, who gets the site? The Third Circuit seems to suggest it went to Quanta, the corporate shell, 739 F.2d, at 914.[17] Presumably, it is an asset that Quanta's creditors can claim, subject, again, to the same question of priority of the rights of the City. Since anyone acquiring the site would have to comply with the clean-up order, however, the site has no value

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17. While this suggests, perhaps erroneously, that the Quanta in bankruptcy is a "different entity" from the Quanta outside of bankruptcy, the effect of this conclusion is that this asset is then an asset of Quanta, the corporate shell. This Court questioned the logic of the "new entity" distinction in NLRB v. Bildisco & Bildisco, 104 S.Ct. 1188, 1197 (1984).

to any of the creditors until cleaned up. That presumably is why the mortgagees abandoned their mortgages. The City spent money to clean up the site; because of that clean-up, the site presumably now has value. One would have thought that because only through the expenditure of money by the City did the site have value, the City gets the property. (It is a lot like a purchase money interest or repairman's lien: the only thing that gave the property value was the expenditure of money by the City of New York. Any owner would gladly give the site to someone who took care of its associated liability.) One would have thought, accordingly, that the property had effectively been abandoned to the City. But if that is so, this is tantamount to a holding that the City of New York has first priority to use the asset to pay for the clean-up: once the clean-up is complete, the City of New York can sell the site to recoup

some of its expenses (Case 2).[18] If this is the effect of abandonment, however, it is perverse to see the City of New York complain about it. By getting first dibs to the asset, the City has, in fact, gotten all out of that site it can.

Presumably, however, the City is objecting to abandonment for another reason. But for abandonment, the City contends, the trustee of Quanta would have had to use as many of Quanta's assets as possible to clean up the site. That, as the analysis above shows, is really only demanding a resolution of the question of the priority of the City relative to the other claimants of Quanta with respect to the remainder of Quanta's assets in line with Case 3. But resolution

18. The bankruptcy court denied the City a prior lien on the site. The effect of this on who owns the site is unexplored, since the City never appealed that order. See note 4 supra. It is hard to see, however, how one could avoid the outcome that the City would own the site, for the reasons discussed in text. But that, of course, is not a bankruptcy issue at all.

of that priority issue is not a question of bankruptcy law, and has nothing whatsoever to do with the subject of abandonment.

The real question in this case is not one of abandonment but, rather, what nonbankruptcy law says about the right of the City to pursue that obligation against Quanta's assets relative to the right of Quanta's other pre-petition creditors. If, under New York (or federal) law, the right is tantamount to an unsecured obligation (Case 1), then the City should share pro rata with Quanta's other unsecured creditors in the property of the estate assembled under 11 U.S.C. § 541. But if, however, under New York (or federal) law, the right is tantamount to a security interest in the remaining assets, then the City is entitled to have that obligation satisfied first out of the property of the estate (Case 3). And that is true whether state law characterizes the obligation as secured, or the subject of

a statutory lien, or a statutory trust. Intermediate solutions (e.g., Case 2) also exist. But bankruptcy law neither answers that question nor provides an obstacle once it is answered.

CONCLUSION

Amicus believes that focusing on the question of abandonment misses the real issue in this case. When a corporation is insolvent, it cannot pay off all its claimants in full. In that circumstance, where all cannot be paid in full, some claimants will fare better than others, because nonbankruptcy law has given them a right to pursue the assets ahead of the claims of others. Bankruptcy law respects this ordering, 11 U.S.C. § 726. If the obligation Quanta owed to the City is, in effect, secured by a lien on all of Quanta's assets, then the City is entitled to have

that obligation satisfied in full. On this key question, one of the relative status of the obligation of the City vis-a-vis the other claimants to Quanta's assets, the opinions below are silent. Since this is a matter of nonbankruptcy law in the first instance, to which bankruptcy law is then applied, amicus respectfully suggests that, unless certiorari is dismissed as improvidently granted, the judgment below be reversed, and the case remanded for consideration of New York (and nonbankruptcy federal) law on this point.

Respectfully submitted.

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Nos. 84-801, 84-805

IN THE UNITED STATES SUPREME COURT

October Term, 1984

MIDLANTIC NATIONAL BANK, Petitioner, v. NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION, Respondent.	)
THOMAS J. O'NEILL, Petitioner, v. CITY OF NEW YORK, Respondent.	)

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

BRIEF OF AMICUS CURIAE PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

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IN THE UNITED STATES SUPREME COURT

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BRIEF OF AMICUS CURIAE PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONERS

INTEREST OF AMICUS

Pursuant to Supreme Court Rule 36, Pacific Legal Foundation respectfully submits this brief amicus curiae in support of petitioners. Consent to the filing of this brief has been granted by counsel for all parties. Copies of the letters of consent have been lodged with the Clerk of this Court.

Pacific Legal Foundation is a nonprofit, tax-exempt corporation, incorporated under the laws of California for the purpose of participating in litigation affecting public policy. An independent Board of Trustees authorizes participation in a case only when it concludes that Pacific Legal Foundation's position has broad public support. The Board of Trustees has authorized the filing of this brief.

Pacific Legal Foundation's public policy perspective in support of private property rights will help provide this Court with a more complete briefing of the interests at stake in this litigation.

OPINION BELOW

The opinions of the United States Court of Appeals are reported at 739 F.2d 912 (3d Cir. 1984), and 739 F.2d 927 (3d Cir. 1984).

STATEMENT OF THE CASE

Quanta Resources Corporation, a company which operated waste oil processing facilities, went into bankruptcy. A trustee was appointed to liquidate the company's assets for distribution to creditors. Among the company's assets were two storage facilities; one located in New York, and one located in New Jersey. Contaminated oil was discovered at both sites, in violation of

state environmental protection laws. The trustee decided that the cost to the estate of cleaning up these facilities exceeded their value. He therefore proceeded to abandon the assets back to Quanta, the party responsible for the violation. New York and New Jersey opposed the abandonment, claiming that the trustee must clean up the facilities, even if that meant using the other assets in the estate to pay for it. The trustee and creditors holding perfected security interests in other assets argued that the Just Compensation Clause of the Fifth Amendment would be violated if the government extinguished these security interests to pay for the cleanup. The Court of Appeals dismissed the "taking" claim in a footnote, stating:

"[W]e are not persuaded by the Trustee's argument

that an unconstitutional taking could result from forbidding abandonment here. ... [T]he state's enforcement of its environmental protection laws cannot be characterized as a taking; rather it is a permissible exercise of the state's regulatory power to promote the public good ...." Matter of Quanta Resources Corp., 739 F.2d at 922 n.11.

It is this summary dismissal of a claim to constitutional protections which amicus curiae wishes to address, because it "flatly contradicts clear

precedents of this Court." San Diego Gas & Electric Co. v. City of San Diego, 450 U.S. 621, 647 (1981) (Brennan, J., dissenting).

SUMMARY OF THE ARGUMENT

The Court of Appeals did not decide whether Quanta's creditors "own" property of the estate to the extent that, if applied to other obligations of the bankrupt, they must be compensated. It never reached this question because the majority apparently concluded that the government's power to regulate for the public good could preempt the protections of the Fifth Amendment. This brief will demonstrate that the authority of government to take property for public use is a police power authority. When a valid exercise of this police power takes a protected

property interest the Fifth Amendment requires the government to compensate the owner or to withdraw the action.

ARGUMENT

I

PRELIMINARY STATEMENT: ISSUE PRESENTED

The Court of Appeals held that if the abandonment were denied, and other assets in the Quanta estate were applied under state law to clean up the New York and New Jersey facilities, it would be unnecessary to analyze whether a "taking" had occurred. The court based this holding on its conclusion that no "taking" could occur, because a state's enforcement of its environmental protection laws is a permissible exercise of the state's "regulatory power to promote the public good," or in other words, its police power. *Matter*

of Quanta Resources Corp., 739 F.2d at 922 n.11.

Amicus takes no position on whether these creditors would be entitled to compensation if the abandonment were denied. That question can be answered only by analyzing whether these creditors have a protected property interest (Webb's Fabulous Pharmacies, Inc. v. Beckwith, 449 U.S. 155, 161 (1980)), which will be sufficiently interfered with so as to cause them to bear an unfair share of a public obligation. Armstrong v. United States, 364 U.S. 40, 49 (1960). Amicus believes, however, that these creditors are entitled to have their claims evaluated by a proper "taking" analysis. The issue thus presented is whether a "taking" could occur when a

state engages in a permissible exercise of its police power.

II

POLICE POWER ACTS THAT AFFECT PROPERTY MUST BE ANALYZED TO DETERMINE WHETHER COMPENSATION IS OWED

The police power is the power of government to serve the people for which it exists. Sporhase v. Nebraska ex rel. Douglas, 458 U.S. 941, 956 (1982). The police power authorizes government to undertake any measure deemed necessary, by the people's elected representatives, to protect the public health, safety, and welfare. Andrus v. Allard, 444 U.S. 51, 59 (1979); Eiger v. Garrity, 246 U.S. 97, 102-03 (1918). The government's authority to take or damage property for public use is one of the government's police power authorities. Hawaii

Housing Authority v. Midkiff, ___ U.S. ___, 81 L. Ed. 2d 186, 196 (1984); Berman v. Parker, 348 U.S. 26, 31-32 (1954). Thus, contrary to the suggestion by the majority of the Court of Appeals, there is no distinction between the government authority to take ownership of property and the authority to regulate that property. The ability to take property is merely a subsidiary power of the government's overall police power.

Governmental activities affecting property, then, are constrained by the same limitations placed on all exercises of the police power; that is, the activity must reasonably promote the public health, safety, or welfare. Hawaii Housing Authority v. Midkiff, 81 L. Ed. 2d

at 197 ("[t]he 'public use' requirement is thus coterminous with the scope of a sovereign's police powers"). Governmental activities affecting property which do not promote public health, safety, or welfare are therefore not permissible exercises of the government's police power. Thompson v. Consolidated Gas Utilities Corporation, 300 U.S. 55, 80 (1937).

On the other hand, governmental activities which do promote the public health, safety, and welfare are valid exercises of the police power regardless of whether such governmental activities take or damage property. Hodel v. Virginia Surface Mining and Reclamation Association, 452 U.S. 264, 300 (1981). When valid exercises of the police power so affect property,

however, the Fifth Amendment requires the government to compensate the owner. In Loretto v. Teleprompter Manhattan CATV Corp., 458 U.S. 419 (1982), this Court recently stated:

> "The Court of Appeals determined that § 828 serves ... legitimate public purpose[s] ... and thus is within the State's police power. We have no reason to question that determination. It is a separate question, however, whether an otherwise valid regulation so frustrates property rights that compensation must be paid." Id. at 425.

Again, in United States v. Security Industrial Bank, 459 U.S. 70

(1982), a case involving issues similar to those at bar, this Court repeated the rule that valid exercises of governmental power may nonetheless require compensation when property is affected.

> "It may be readily agreed that § 522(f)(2) is a rational exercise of Congress' authority .... Such agreement does not, however, obviate the additional difficulty that arises when that power is ... used to defeat traditional property interests. The bankruptcy power is subject to the Fifth Amendment's prohibition against taking private property without compensation. ... Thus, however 'rational' the exercise of the

> bankruptcy power may be, that inquiry is quite separate from the question whether the enactment takes property [so as to require compensation]."
>
> United States v. Security Industrial Bank, 459 U.S. at 74-75.

The distinction between government action to regulate property and government action to take ownership in property is not, as suggested by the majority of the Court of Appeals, a distinction in the source or validity of the authority; rather, the distinction is in the remedy. An invalid exercise of the police power will be set aside, but when property is taken or damaged by valid regulation, the government is entitled to keep the property, or

inflict the damage, so long as it compensates the owner. Ruckelshaus v. Monsanto Co., ___ U.S. ___, 81 L. Ed. 2d 815, 841 (1984). Such compensation must be available "to bar Government from forcing some people alone to bear public burdens which, in all fairness and justice, should be borne by the public as a whole." Armstrong v. United States, 364 U.S. at 49; Penn Central Transportation Co. v. City of New York, 438 U.S. 104, 124 (1978). If government can "pre-empt" property rights by merely exercising its police power, "then the Taking Clause has lost all vitality." Ruckelshaus v. Monsanto Co., 81 L. Ed. 2d at 838.

Applying this body of law to the case at bar, the secured creditors

of Quanta have claimed a property interest in the assets of Quanta's estate which will be "taken" if abandonment of the New Jersey and New York facilities is disallowed. This claim of a "taking" does not arise from the direct application of the states' environmental laws. It arises from the potential transfer of liability from the culpable party to innocent creditors by requiring the trustee to accept responsibility for the cleanup costs. Therefore, contrary to the suggestion by the majority of the Court of Appeals, this case does not present a conflict between environmental regulation and protection of private property rights. The creditors do not argue that the environmental laws should not be enforced; their claim is that their

protected property interests may be taken. Having raised this claim, they are entitled to have a court analyze whether their claim is meritorious. The Court of Appeals, however, did not analyze whether the creditors have a valid "taking" claim. It avoided this question by finding that the states' enforcement of environmental protection laws was a valid exercise of their police power. The determination of the "taking" claim, however, should not turn on an analysis of the regulatory power employed. The question is whether the creditors would lose a protected property interest and be forced to bear more than their fair share of a public obligation. If so, compensation to

those individuals would be owed. <u>United States v. General Motors Corp.</u>, 323 U.S. 373, 378 (1945).

CONCLUSION

For the reasons set forth above amicus requests this Court to expressly disapprove the Court of Appeals' conclusion that prohibiting abandonment cannot raise the question of an uncompensated taking of a protected property interest in violation of the protections of the Fifth Amendment.

DATED: April 5, 1985.

Respectfully submitted,

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DECLARATION OF SERVICE BY MAIL

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I am a citizen of the United States, residing or employed in Sacramento, California.

My business address is 555 Capitol Mall, Suite 350, Sacramento, California.

I am over the age of 18 years, and am not a party to the above-entitled action.

On April 5, 1985, true copies of BRIEF OF AMICUS CURIAE PACIFIC LEGAL FOUNDATION IN SUPPORT OF PETITIONERS were placed in envelopes addressed to:

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which envelopes, with postage thereon fully prepaid, were then sealed and deposited in a mailbox regularly maintained by the United States Postal Service in Sacramento, California.

I declare under penalty of perjury that the foregoing is true and correct and that this declaration was executed this 5th day of April, 1985, at Sacramento, California.

/s/ LINDA S. SCHAUPP

LINDA S. SCHAUPP

(8) (7)

Nos. 84-805 and 84-801

IN THE

Supreme Court of the United States

OCTOBER TERM, 1984

THOMAS J. O'NEILL, TRUSTEE IN BANKRUPTCY OF QUANTA RESOURCES CORPORATION, Debtor,
Petitioner,

v.

THE CITY OF NEW YORK and STATE OF NEW YORK,
Respondents.

MIDLANTIC NATIONAL BANK,
Petitioner,

v.

NEW JERSEY DEPARTMENT OF ENVIRONMENTAL PROTECTION,
Respondent.

On Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF OF THE STATE OF WEST VIRGINIA AND FIFTEEN STATES AS *AMICI CURIAE*

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BRIEF OF THE STATE OF WEST VIRGINIA AND FIFTEEN STATES AS *AMICI CURIAE*

THE INTEREST OF THE *AMICI CURIAE*

The *amici curiae* are the Attorneys General of the State of West Virginia and the states of Indiana, Texas, Oklahoma, Delaware, Pennsylvania, Connecticut, Tennessee, Ohio, New Mexico, North Carolina, Michigan, New Hampshire, Vermont, Kansas and Illinois, who file this brief pursuant to Rule 36.4 of the Rules of the Supreme Court of the United States. In each of the *amici* states, the governors and the legislatures have developed or are developing comprehensive statutory and regulatory programs for assuring the public health, safety and welfare by protecting the environment.[1]

Crucial to such state programs are state statutes and city ordinances intended to impose liability for abatement and rehabilitation upon the polluter who violates these laws and thereby causes serious environmental harm. The United States Court of Appeals for the Third Circuit correctly recognized the importance of such laws and reversed the courts below it, remarking "[t]hat Congress did not intend to abrogate the enforcement of state police power regulations . . ." 739 F.2d 912, 918. When the bankruptcy courts allow abandonment and thereby relieve illegal operators such as Quanta, and their legal successors, the trustees in bankruptcy, of precisely such responsibility, the bankruptcy courts effectively nullify those state programs and jeopardize the public health and safety. The decision of the United States Court of Appeals for the Third Circuit prohibiting such a result should be affirmed.

[1] West Virginia's statutes are illustrative of the comprehensive program of environmental protection. Each statute is designed to address a particular area of concern. West Virginia Water Pollution Control Act, W. Va. Code § 20-5A-1 *et seq.*, 1981, 1984 Supp. (Water Pollution); West Virginia Air Pollution Control Act, W. Va. Code § 16-20-1 *et seq.*, 1985 (Air Pollution); West Virginia Hazardous Waste Management Act, as amended, W. Va. Code § 20-5E-1 *et seq.*, 1981, 1984 Supp. (Hazardous Waste); West Virginia Solid Waste Management Act, as amended, W. Va. Code § 20-5F-1 *et seq.*, 1981, 1984 Supp. (Solid Waste); West Virginia Surface Coal Mining and Reclamation Act, W. Va. Code § 20-6-1 *et seq.*, 1981, 1984 Supp. (Surface Mining).

The common interest of the *amici* lies in the preservation of their ability to protect the citizenry through enforcement of state police power enactments. They also seek to vindicate the Congressional intent that the Bankruptcy Code honor, rather than undermine, the legitimate interest of the states in seeking the abatement of hazards and nuisances which threaten the public health, safety and welfare. *The amici* have a growing concern that lower federal courts are failing as federal courts of equity by allowing bankrupts to subvert these important state interests.

In recent years, Congress has increasingly recognized the importance of protecting the same interests served by the state environmental protection statutes.[2] The comprehensive regulatory scheme enacted by Congress is designed to protect against, *inter alia*, existing and past unlawful hazardous waste disposal activities and includes provisions for state enforcement of various federally imposed requirements. If the Third Circuit's decision is reversed, that scheme could be impaired severely. The *amici* also have an interest in protecting the effectiveness of the federal programs and the ability of the states to enforce the provisions of those laws.

SUMMARY OF ARGUMENT

The United States Court of Appeals for the Third Circuit protected the public health and safety and vindicated Congressional policy under the Bankruptcy Code by refusing to allow the bankrupt Quanta Resources to abandon its responsibilities with respect to two dangerous hazardous waste disposal sites.

[2] *See, e.g.*, the Clean Air Act, 42 U.S.C. § 7401; the Federal Water Pollution Control Act, 33 U.S.C. § 1251; the Resource Conservation and Recovery Act, 42 U.S.C. § 6901; the Federal Surface Mining Control and Reclamation Act, 30 U.S.C. § 1201; the Comprehensive Environmental Response, Compensation and Liability Act (Superfund legislation), 42 U.S.C. § 9601.

Even assuming that Congress may have granted the federal bankruptcy courts a new statutory power to overrule the states' exercise of the police power reserved to them under the Tenth Amendment, to jeopardize the public health and safety, to ignore the intent of the Bankruptcy Code and to disregard the federal legislative scheme controlling and regulating hazardous waste, it is manifestly clear that the Constitution requires that such power must be exercised, if ever, in a manner consistent with the balancing of interests required of a federal court sitting in equity, rather than as a purely commercial tribunal whose sole interest lies in the vindication of creditors' rights. The United States Court of Appeals for the Third Circuit properly reversed such an untoward result and should be affirmed.

ARGUMENT

The United States Court of Appeals for the Third Circuit protected the public health and safety and vindicated Congressional policy under the Bankruptcy Code by refusing to allow the bankrupt Quanta Resources to abandon its responsibilities with respect to two dangerous hazardous waste disposal sites.

By interfering with the legitimate efforts of New York, New York City and New Jersey to contain and control severe environmental hazards by compelling the bankrupt to comply with state and local laws respecting environmental protection, the bankruptcy court imperiled the public health and safety in the vicinity of the two sites. The United States Court of Appeals for the Third Circuit correctly reversed the courts below, remarking: "[c]onsidered in the light of other provisions that both limit the supersession of state laws and specifically incorporate equitable principles into a bankruptcy court's jurisdiction, it is clear that Section 554 [of the Bankruptcy Code] does not of itself preempt state police power regulations." 739 F.2d 912, 918 (3rd Cir. 1984).

Despite state statutes and city ordinances clearly intended to impose liability for abatement and rehabilitation upon the polluter who violates these laws and thereby causes serious environmental harm, the bankruptcy court in fact relieved Quanta—just such an illegal operator—and its legal successor, the trustee in bankruptcy, of precisely such responsibility.

State regulatory agencies throughout the nation are faced every day with the urgent need to protect their citizens from both the immediate dangers posed by the illegal disposal of hazardous and industrial waste, as in the instant cases, and by violations of the other state statutes[3] designed to protect the public health, safety and welfare. Such statutes represent valid exercises of the police power, reserved to the states under the Tenth Amendment to the Constitution of the United States. Traditionally recognized by this Court as the least limitable of the reserved powers, *Queenside Hills Realty v. Saxl*, 328 U.S. 80 (1946), the police power broadly authorizes the various states to regulate in order to protect the health, safety and welfare of their citizens.

Legitimate state enforcement action pursuant to such statutes is thwarted when illegal activities are sanctioned by the federal bankruptcy courts. In the instant cases, the federal bankruptcy court refused to show constitutionally mandated deference toward the states in the exercise of the police power. The decision of the United States Court of Appeals for the Third Circuit correctly redressed this imbalance, by reversing the courts below and refusing to allow abandonments which result in violations of the state laws and city ordinances concerning the disposal of hazardous waste.

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[3] The briefs of New York, New York City and New Jersey are replete with reference to the various state and municipal requirements relating to police power enactments respecting environmental protection. *See* n.1, *supra*.

Quanta's trustee in bankruptcy is under an absolute and unconditional obligation to comply with the laws of New York, New York City and New Jersey, and to apply all necessary assets of the estate to the cleanup of the two environmental disasters which Quanta owned and in the creation of which Quanta aided. The Bankruptcy Code itself contemplates that state police power actions will not be subjected to interference by the federal bankruptcy courts, *see* 11 U.S.C. § 362 (b)(4); 28 U.S.C. § 1478(a).[4] The trustee must comply with validly enacted state police power statutes, 28 U.S.C. § 959 (b). As the United States Court of Appeals for the Third Circuit remarked: "[t]he question thus presents itself: did Congress intend that the trustee's abandonment power be unrestricted by public health and safety regulations? Our examination of the bankruptcy laws and the authorities interpreting these laws reveals no such congressional intent." 739 F.2d 912, 916.

Furthermore, the action of the bankruptcy court was at marked variance with clearly expressed congressional intent respecting environmental protection against the illegal disposal of hazardous waste, *see, e.g.*, 42 U.S.C. §§ 6901(b)(4) and 6901(b)(5). The United States Court of Appeals for the Third Circuit specifically recognized that state and local law implement the same intent: "[t]he primary purpose of the state and local laws regulating the disposal of hazardous wastes is obviously to protect the public from the toxic effect of dangerous substances by preventing their uncontrolled discharge into the environment." 739 F.2d 912, 915 (3rd Cir. 1984).

The action of the bankruptcy court frustrated the operation and administration of the federal laws concerning the protection of the public against the dangers posed

[4] Section 1478 of Title 28 was modified by the Bankruptcy Amendments and Federal Judgeship Act of 1984, P.L. 98-353. However, the policy protecting states from removal remained the same.

by the illegal disposal of dangerous industrial waste. Given the bankruptcy court's failure to respect the reserved police power of New York and New Jersey, and given its obstruction of the operation and administration of the federal environmental law, the decisions of the Bankruptcy Court were properly reversed, and the decision of the United States Court of Appeals for the Third Circuit should be affirmed.

The United States Court of Appeals for the Third Circuit correctly required the bankruptcy court to carry out its obligations as a federal court of equity by balancing the public health, safety and welfare against the financial interests of Quanta's creditors.

The bankruptcy court below also failed as a federal court of equity.[5] The United States Court of Appeals for the Third Circuit properly identified the bankruptcy court as just such a court, 739 F.2d 912, 917, and proceeded to present the balancing of equities which the bankruptcy court should have, but here failed, to do:

> In this case, the state and local regulations advance a very important policy: to protect the public health by regulating disposal of toxic wastes. *Abandonment by the trustee clearly contravened applicable law, and did so not merely technically, but with severely deleterious implications for the public safety. . .*
>
> To be weighed against this manifestly important public policy is the policy advanced by abandonment, to preserve as much of the estate as possible for distribution to creditors. This policy must be viewed in light of the indications of a concurrent federal legislative policy to limit intrusion into state police power regulations, including environmental protection laws. . .

[5] *See Ottenheimer v. Whitaker*, 198 F.2d 289 (4th Cir. 1952); *In re Lewis Jones, Inc.*, 1 Bkr. Ct. Dec. 277 (E.D. Pa. 1974), which were cited with approval by the United States Court of Appeals for the Third Circuit, 739 F.2d 912, 916-918 (1984).

> But the extent (unproven in these proceedings) of the expenditures necessary to dispose of the waste properly is not in itself sufficient to outweigh the public interest at stake here. . . The supremacy clause does not require the suspension of the operation of New York's hazardous waste disposal laws. 739 F.2d 921-922 (footnotes omitted) (emphasis supplied).

As a court of equity, the bankruptcy court below succeeded only in protecting the limited group of entities which financed the creation of the two illegal hazardous waste disposal sites. It provided no consideration or protection for the citizenry actually or potentially affected by the illegal hazardous waste, and it chose to impose indirectly the costs of cleanup upon the already strained fisc of New York, New York City and New Jersey.

Were the trustee compelled to address his responsibilities with respect to the Quanta sites, the various creditors who financed the creation of the Quanta disasters would have nothing legitimate to complain of. A prudent lender is on inquiry notice with respect to real estate security, and such a lender ought logically at least on occasion to police such collateral. Even assuming that the creditors were unaware of the illegal conduct on the part of their debtor, this Court has sustained actions by governmental agencies which worked far more onerous deprivations without finding a compensable taking. For example, in *Astol Calero-Toledo v. Pearson Yacht Leasing Company*, 416 U.S. 663 (1974), a yacht lessor's boat was seized and forfeited by the authorities of Puerto Rico pursuant to the arrest of a dealer in illegal drugs who was using the boat to transport drugs. Despite the yacht lessor's complete lack of knowledge of or connection with the criminal enterprise, this court held that no unconstitutional deprivation was worked by the forfeiture.

Finally, the bankruptcy court below proceeded as though totally unaware that the state statutes and ordinances involved in the instant cases (as well as their equivalents in West Virginia and other states) were enacted to implement and complement federal legislative action under the Commerce Clause.[6] The constitutional scheme protecting both the police power of the states and the power of the federal government to regulate interstate commerce was severely disrupted when the bankruptcy court below allowed abandonment to proceed.

The United States Court of Appeals for the Third Circuit has set forth a lucid and sensible analysis for bankruptcy courts to apply when they consider abandonments which may involve violations of state and local laws respecting the disposal of hazardous waste. On the one hand, the court must consider ". . . a very important policy: to protect the public health by regulating disposal of toxic wastes." 739 F.2d 912, 921. On the other hand, the court must consider ". . . the policy advanced by abandonment, to preserve as much of the estate as possible for distribution to creditors." 739 F.2d 912, 921. Where the two policies conflict, the court must rule in favor of the public health, safety and welfare. As the United States Court of Appeals for the Third Circuit concluded: "[t]he Supremacy clause does not require the suspension of New York's hazardous waste disposal laws." 739 F.2d 912, 921. Its judgments should be confirmed.

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[6] *See, e.g.*, the Resource Conservation and Recovery Act, 42 U.S.C. § 6901 *et seq.*; the Clean Air Act, 42 U.S.C. § 7401 *et seq.*; the Water Pollution Control Act, 33 U.S.C. § 1251 *et seq.* and the Surface Mining Control and Reclamation Act, 30 U.S.C. § 1201 *et seq. See also*, Wein, *Environmental Regulation and the Bankruptcy Act*, 17 *Duq. L. Rev.* 133, 136 (1978-1979).

CONCLUSION

The United States Court of Appeals for the Third Circuit protected the public health and safety and vindicated Congressional policy under the Bankruptcy Code by refusing to allow the bankrupt Quanta Resources to abandon its responsibilities with respect to two dangerous hazardous waste disposal sites. The United States Court of Appeals for the Third Circuit correctly required the bankruptcy court to carry out its obligations as a federal court of equity by weighing the public health, safety and welfare against the financial interests of Quanta's creditors.

Accordingly, the judgments of United States Court of Appeals for the Third Circuit should be affirmed.

Respectfully submitted,

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v.

CITY OF NEW YORK, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING RESPONDENTS

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QUESTION PRESENTED

Whether a bankruptcy trustee's power to abandon property that is a financial burden to the bankruptcy estate is subject to generally applicable law safeguarding public health and safety.

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v.

CITY OF NEW YORK, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE THIRD CIRCUIT

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING RESPONDENTS

INTEREST OF THE UNITED STATES

The reach of the Bankruptcy Code is once again tested by the financial distress of a debtor that handled hazardous wastes. Compare *Ohio* v. *Kovacs*, No. 83-1020 (Jan. 9, 1985). The question presented in this case, whether

the trustee of a bankrupt company may abandon financially burdensome hazardous wastes and related property free from state law constraints, implicates multi-faceted federal concerns. As an initial matter, the United States administers the Bankruptcy Code's pilot program for United States Trustees. See 11 U.S.C. 1501 *et seq.* The United States thus recognizes the trustee's central and, indeed, essential role under the Code and has a fundamental interest in this Court's interpretation of the trustee's abandonment power. But the United States also enforces a broad range of public health and welfare statutes [1] and is therefore attentive to the states' legitimate rights to protect the health and safety of their citizenry. Federal environmental statutes, although not at issue in this case, typically complement state laws and frequently are implemented through a federal-state partnership,[2] embrace basic principles of federalism and rely heavily on the states' exercise of traditional police powers.

The United States has a particularly acute interest in this case on account of its activities at the debtor's waste site in Edgewater, New Jersey. The United States Environmental Protection Agency, recognizing that the Edgewater site poses a serious risk to public health and safety, has initiated an emergency removal action under Section 104 of the Comprehensive Environmental Response, Compensation, and Liability Act of 1980 (CERCLA), 42 U.S.C. 9604, to alleviate immediate public health risks at

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[1] *E.g.,* Clean Water Act of 1977, 33 U.S.C. 1251 *et seq.*; Clean Air Act, 42 U.S.C. 7401 *et seq.*; Toxic Substances Control Act, 15 U.S.C. 2601 *et seq.*; Resource Conservation and Recovery Act of 1976, 42 U.S.C. 6901 *et seq.*; and Comprehensive Environmental Response, Compensation, and Liability Act of 1980, 42 U.S.C. 9601 *et seq.*

[2] See, *e.g.,* Resource Conservation and Recovery Act of 1976, 42 U.S.C. 6921, 6926, 6929, 6931; Comprehensive Environmental Response, Compensation, and Liability Act of 1980, 42 U.S.C. 9604(c) and (d), 9605, 9611(f), 9614.

the site.[3] EPA also is contemplating actions for reimbursement of its cleanup costs from potentially responsible parties.

STATEMENT

Quanta Resources Corporation, a Delaware corporation formed in March 1980, operated three waste oil recovery facilities located, respectively, in Edgewater, New Jersey; Long Island City, New York; and Syracuse, New York. Environmental conditions at the Edgewater and Long Island City facilities are at the center of the present dispute.

Quanta acquired the Edgewater facility in July 1980 through the purchase of the assets of Edgewater Terminals, Inc. By that purchase, Quanta received a lease of the underlying real property, outright ownership of the facility and its inventory, and an assignment of the temporary permit issued by the New Jersey Department of Environmental Protection (NJDEP). On June 3, 1981, petitioner Midlantic National Bank (Midlantic) provided Quanta with a $600,000 working capital loan secured by Quanta's inventory, accounts receivable, and certain equipment.

Quanta acquired the Long Island City facility through the purchase of the assets of Hudson Oil Refining Corporation. By that purchase, Quanta acquired an owner-

---

[3] EPA became involved at the site following an April 18, 1984, request from the New Jersey Department of Environmental Protection for application of "Superfund" monies, see 42 U.S.C. 9631, available under CERCLA, see 42 U.S.C. 9604, 9611, to institute an immediate removal of hazardous materials from the site. EPA, acting on an investigation by its Regional Office and a review by the Centers for Disease Control, concluded that the site posed an immediate risk of harm to public health and welfare and authorized the expenditure of $4,460,000 to commence removal actions. See 42 U.S.C. 9601(23). Copies of New Jersey's April 18, 1984, funding request, the EPA Regional Office's January 25, 1985, action memorandum, the Centers for Disease Control's March 2~~5~~2, 1985, hazard determination, and EPA's approval memorandum have been lodged with the Court.

ship interest in the real property (subject to two mortgages totalling $454,464), the facility, and its inventory. Quanta also became subject to a consent order with the New York Department of Environmental Conservation requiring Quanta to bring the facility into compliance with state environmental law.

In June 1981, some time after Quanta received the Midlantic loan, an NJDEP inspection at the Edgewater facility uncovered unlawful concentrations of polychlorinated biphenyls (PCBs), which are extremely toxic carcinogens, in Quanta's waste oil inventory. The presence of PCBs violated Quanta's operating permit; accordingly, in July 1981, Quanta ceased its Edgewater operations at NJDEP's request. Quanta and NJDEP engaged in negotiations concerning cleanup of the property. However, on October 6, 1981, Quanta filed a petition for reorganization under Chapter 11 of the Bankruptcy Code. On October 7, 1981, NJDEP ordered Quanta to clean up the hazardous wastes at the Edgewater site. On November 11, 1981, Quanta filed for conversion of the Chapter 11 proceeding to a Chapter 7 liquidation and, on November 18, 1981, petitioner Thomas J. O'Neill was appointed liquidation trustee (the Trustee). PCB contamination at the Long Island site was apparently discovered some time after Quanta filed for bankruptcy.

At the time of the bankruptcy filing, the Edgewater facility's inventory included approximately 3.5 to 5.0 million gallons of waste oil, of which approximately 400,000 gallons were contaminated with PCBs. The Long Island City facility's inventory included approximately 500,000 gallons of waste oil, of which approximately 70,000 gallons were contaminated with PCBs. It appears that the PCB contamination extended to the soil and subsoil portions of both sites.

The Trustee attempted without success to sell the Long Island City site for the benefit of Quanta's creditors. On May 25, 1982, the Trustee notified the creditors that he intended to abandon the site pursuant to Section 554 of

the Bankruptcy Code.[4] The City and State of New York (New York) objected, contending that abandonment would threaten public health and safety. The bankruptcy court nonetheless approved the abandonment (Pet. App. 73a-74a).

New York appealed the bankruptcy court's order to the district court and, meanwhile, in response to the public health threat, initiated cleanup of the site. The district court, although noting that "the question is a close one," later affirmed the bankruptcy court's abandonment order (Pet. App. 56a). Shortly thereafter, on May 20, 1983, the bankruptcy court authorized the Trustee to abandon the PCB-contaminated waste contained in storage tanks at the Edgewater facility, despite NJDEP's objections (*id.* at 64a-65a).

New York and NJDEP petitioned the court of appeals for review, respectively, of the district court's judgment and the bankruptcy court's May 20, 1983, abandonment order. On July 20, 1984, a divided panel of the court of appeals reversed both decisions (Pet. App. 1a-35a). The court concluded that the Trustee's abandonment powers under Section 554 of the Bankruptcy Code are subject to state health and safety laws and remanded the case for further proceedings. The dissent agreed with the lower courts that Section 554 gives the Trustee absolute power to abandon property that, from the creditors' perspective, is financially burdensome.

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[4] Section 554(a), 11 U.S.C. 554(a), as then in force, provided in part:

> After notice and a hearing, the trustee may abandon any property of the estate that is burdensome to the estate or that is of inconsequential value to the estate.

This language was changed slightly by the 1984 Bankruptcy Amendments, but the amendments did not affect the substance of the provision. See Pub. L. No. 98-353, 98 Stat. 333 *et seq.* Abandonment under Section 554 transfers title to the property from the bankruptcy estate to any party with a possessory interest (typically, the debtor). See 11 U.S.C. 554 note. See also 11 U.S.C. 722.

SUMMARY OF ARGUMENT

The present conflict has been presented largely as a choice between extremes: the Trustee has demanded unfettered discretion to abandon hazardous wastes and related property, while respondents, at least in the initial proceedings, have demanded that the Trustee assume total responsibility for the dangerous conditions. Such absolutism is neither necessary nor desirable. The court of appeals' judgments, holding that the Trustee's abandonment power is limited by state police powers, reasonably accommodates both the Bankruptcy Code and public health interests and finds full support in the principles of equity and fairness that underlie the federal bankruptcy laws.

It has been long established, in a variety of contexts, that a bankruptcy trustee must administer a bankruptcy estate in compliance with federal and state law unless the Bankruptcy Code, by its express terms or necessary implication, displaces or overrides the otherwise applicable law. Indeed, the reach of the Bankruptcy Code is governed by traditional principles of preemption, which require that federal law accommodate state law to the extent that it is possible and consistent with the full purposes of Congress. Moreover, 28 U.S.C. 959(b) specifically requires the trustee to "manage and operate" property within his possession in accordance with state law. The requirement applies not only to actions taken by the trustee in the course of reorganizing an ongoing business, but also to his actions taken in the course of liquidation.

Thus, the issue before this Court is whether Section 554 of the Bankruptcy Code, 11 U.S.C. 554, which authorizes a trustee to abandon financially burdensome property, creates an exception to established law by preempting generally applicable state law safeguarding the public's health and safety. The answer lies in the history and purpose of the abandonment provision. Congress enacted Section 554 as a codification of a judge-made rule

recognizing a trustee's power to abandon burdensome property. It thereby incorporated within Section 554 the judicially-recognized limitations on that power. The courts, prior to enactment of Section 554, had unequivocally recognized that the trustee's abandonment authority was subject to general police powers. Accordingly, a trustee acting pursuant to Section 554 is subject to the same limitation. This result is completely consistent with the purposes underlying the abandonment power. It preserves the trustee's ability to avoid wasteful and unnecessary transaction costs, while recognizing that his administration of the estate must be conducted in accordance with generally applicable law.

Petitioners' contention that a trustee's abandonment authority is absolute must therefore fail. The court of appeals correctly concluded that a trustee's abandonment authority is subject to traditional state police power limitations. Although specific state environmental statutes such as those suggested by the court of appeals may impose relevant limitations in certain cases, we believe that state public nuisance law provides the clearest and most flexible limitation on a trustee's abandonment authority in a case such as this one. The relevant nuisance principles do not absolutely proscribe abandonment. Instead, they require that the trustee, prior to abandonment, take steps that are reasonable, in light of conditions at the hazardous waste site and the resources of the bankruptcy estate, to ensure that discharge of the property from his custodial care will not create or aggravate a threat to public health and safety. The application of traditional nuisance principles to the facts at hand finds solid support in state law. Additionally, it is consistent with the bankruptcy courts' traditional practice of accommodating competing interests. In all events, petitioners' claim that the application of state law threatens an unconstitutional taking of creditors' property rights is meritless. Thus, the United States urges affirmance of the court of appeals' judgments but suggests a somewhat different interpretation of the applicable state law.

ARGUMENT

A BANKRUPTCY TRUSTEE'S ABANDONMENT OF HAZARDOUS WASTES AND RELATED PROPERTY IS SUBJECT TO GENERALLY APPLICABLE STATE LAW SAFEGUARDING PUBLIC HEALTH AND SAFETY

The Bankruptcy Code charges the bankruptcy trustee with specific enumerated duties and concomitant powers in liquidation proceedings, giving him extensive control over the management of the estate. See *CFTC* v. *Weintraub*, No. 84-261 (Apr. 29, 1985), slip op. 8. The states, meanwhile, have extensive and long-recognized powers to protect the public health and welfare.[5] The trustee and the states thus exercise firmly established authority within their respective spheres and, together, they have enjoyed a relatively peaceful co-existence. However, the special problems presented by the instant dispute—the potentially enormous costs of hazardous waste cleanup and the frightening threats to public health and safety—have brought these powers into ostensibly sharp confrontation. Nonetheless, the clash seems largely the result of the rather extreme positions advanced below: the Trustee has demanded unfettered discretion to abandon the hazardous wastes and related property without regard to resulting public health and safety consequences; meanwhile, respondents, at least in the initial proceedings, demanded that the Trustee assume total responsibility for the hazardous conditions. These polar positions are inconsistent with the general policies of bankruptcy and have created a confrontation where none should exist.[6]

[5] *E.g., Hawaii Housing Authority* v. *Midkiff*, No. 83-141 (May 30, 1984), slip op. 9-10; *Village of Euclid* v. *Ambler Realty Co.*, 272 U.S. 365, 387-388 (1926); *Lawton* v. *Steele*, 152 U.S. 133, 136 (1894); *Mugler* v. *Kansas*, 123 U.S. 623, 668-669 (1887).

[6] As the House Report on the 1978 Bankruptcy Reform Act noted, "[b]ankruptcy law cuts across many other areas of the law. In the interaction between bankruptcy law and other laws, each bends

Instead, the present clash can be comfortably resolved through a careful reading of the particular requirements of federal and state law.

A. A Bankruptcy Trustee Must Administer The Bankruptcy Estate In Compliance With Federal And State Non-Bankruptcy Law Unless The Bankruptcy Code, By Its Express Terms Or Necessary Implication, Displaces Or Preempts The Otherwise Applicable Law

The Bankruptcy Code does not grant the trustee any general power to avoid compliance with non-bankruptcy law. Thus, like any other entity, he must generally comply with such law in discharging his duties.[7] Indeed, this Court has long recognized that if Congress wished to grant the trustee any extraordinary exemption from non-bankruptcy law, "the intention would be clearly expressed, not left to be collected or inferred from disputable considerations of convenience in administering the estate of the bankrupt." *Swarts* v. *Hammer*, 194 U.S. 441, 444 (1904).[8]

somewhat to accommodate the policies of the other." H.R. Rep. 95-595, 95th Cong., 1st Sess. 228 (1977). See, *e.g., NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 10-12.

[7] See *Ohio* v. *Kovacs*, No. 83-1020 (Jan. 9, 1985), slip op. 10 (trustee "in possession" of a hazardous waste site must comply with state environmental laws); *Otte* v. *United States*, 419 U.S. 43, 52 (1974) (trustee must comply with IRS recordkeeping requirements); *Swarts* v. *Hammer*, 194 U.S. 441, 444 (1904) (trustee must pay state and local property taxes, because "there is nothing in [his trust responsibilities] to withdraw [the property] from the necessity of protection by the State and municipality, or which should exempt it from its obligations to either").

[8] See also *NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 19 ("[T]he debtor-in-possession is not relieved of all obligations under the [National Labor Relations Act] simply by filing a petition for bankruptcy."); *Palmer* v. *Massachusetts*, 308 U.S. 79, 85 (1939) ("If this old and familiar power of the states [over local railroad service] was withdrawn when Congress gave district courts bankruptcy powers over railroads, we ought to find language fitting for so drastic a change."); *Penn Terra, Ltd.* v.

The Bankruptcy Code does specify principles for estate administration that can override conflicting non-bankruptcy law (see *Perez* v. *Campbell*, 402 U.S. 637 (1971)), and a conflict, if truly present, must be resolved through a traditional preemption analysis (*id.* at 649-652). But not every intersection of federal bankruptcy law and state law creates a conflict. Indeed, Section 959(b) of the Judicial Code has largely eliminated the possibilities for conflict between the bankruptcy trustee's exercise of his statutory authority and otherwise applicable state law. That section expressly subjects the trustee to state police power (28 U.S.C. 959(b)):

> [A] trustee * * * shall manage and operate the property in his possession as such trustee * * * according to the requirements of the valid laws of the State in which such property is situated, in the same manner that the owner or possessor thereof would be bound to do if in possession thereof.

Petitioners contend that Section 959(b) is relevant only when the trustee is actually operating the business of the debtor, and not when he is liquidating it (84-801 Br. 23-24; 84-805 Br. 22-23). But this contention is inconsistent with the language, legislative history, and purposes of Section 959(b).

Section 959(b) addresses both management and operation of property. Courts "are obliged to give effect, if possible, to every word Congress used," *Reiter* v. *Sonotone Corp.*, 442 U.S. 330, 339 (1979), and Section 959(b), on its face, encompasses something more than "operation." [9] As the court of appeals noted (Pet. App. 17a),

Dep't of Environmental Resources, 733 F.2d 267, 273 (3d Cir. 1984).

[9] Indeed, if Congress had wanted to restrict Section 959(b) to the operation of a business, it would have used the phrase "carrying on business," as it did in Section 959(a). It has been held that that phrase is limited to actions taken in the operation of a business. *Austrian* v. *Williams*, 216 F.2d 278, 285 (2d Cir. 1954), cert. denied, 348 U.S. 953 (1955).

there is no reason why the phrase " 'manage[ment]' of the 'property,' " could not, in the abstract, describe a trustee's custodial care and disposition of property in a bankruptcy liquidation. Indeed, Congress typically uses the term "manage" in conjunction with the term "trustee" to describe a trustee's general activities in administering the trust corpus.[10] Thus, Section 959(b)'s use of the term "manage," evaluated on its face, includes the bankruptcy trustee's general administration of property in his possession, including actions taken in liquidation of the estate.

The legislative history of Section 959(b) supports this conclusion. Section 959(b) originated in state objections raised in the late 19th century against perceived abuses of federal railroad receiverships.[11] Congress, responding to these concerns, adopted a provision expressly subjecting receivers to state law. Act of Mar. 3, 1887, ch. 373, § 2, 24 Stat. 554. See 18 Cong. Rec. 2542-2543 (1887). This provision eventually evolved into the present requirements

[10] See, *e.g.*, 2 U.S.C. 702(e)(3)(C)(i) (blind trusts for public officials); 5 U.S.C. App. 202(f)(3)(C)(i) (same); 29 U.S.C. 1103(a), 1105(b)(2)(B) and (c)(3) (employee benefit plan trusts). This Court follows that practice as well. See *CFTC* v. *Weintraub*, slip op. 8 (emphasis added) (stating, after surveying the trustee's various powers, that "the Bankruptcy Code gives the trustee wide-ranging *management authority* over the debtor").

[11] The railroad receivership was an invention of federal equity courts designed initially to prevent piecemeal foreclosure of financially embarrassed interstate railroads. See generally 3 R. Clark, *The Law and Practice of Receivers* §§ 847-884 (3d ed. 1959). Receivers were expected "to operate such roads, until the difficulties are removed, or such arrangements are made that the roads can be sold with the least sacrifice of the interests of those concerned." *Davis* v. *Gray*, 83 U.S. (16 Wall.) 203, 220 (1872). However, the states charged that the receivers, operating under the aegis of the federal courts, frequently evaded or ignored legitimate state powers, rights, and interests. See S. Misc. Doc. 44, 50th Cong., 1st Sess. (1888); S. Misc. Doc. 7, 50th Cong., 1st Sess. (1887); S. Misc. Doc. 19, 49th Cong., 2d Sess. (1886); H.R. Misc. Doc. 45, 49th Cong., 1st Sess. (1886).

of Section 959(b).[12] The origins of the section demonstrate that it was enacted to prevent federal receivers, and later trustees, from encroaching on general state prerogatives, not only in the operation of a business, but also in pursuing a liquidation. Notably, the equity receivership was a debt management scheme that frequently contemplated either partial or complete liquidation of assets.[13] Indeed, at the time that the original provision was enacted, federal law did not expressly provide for debtor reorganization, and partial or complete foreclosure was the likely prospect.[14] And in all events, particular conduct

[12] The provision has been reenacted on several occasions, but its basic substance has remained unchanged. For present purposes, we need note only two of the amendments. The provision was first codified at 28 U.S.C. 124 (see Section 65 of the Act of Mar. 3, 1911, ch. 231, 36 Stat. 1104). In 1948, it was amended to apply to trustees and debtors-in-possession and recodified at 28 U.S.C. 959(b). See Judiciary Act of 1948, ch. 646, 62 Stat. 927; H.R. Rep. 308, 80th Cong., 1st Sess. A102 (1947).

[13] See generally G. Glenn, *The Law Governing Liquidation* §§ 149-172 (1935); 7 *Moore's Federal Practice*, Pt. 2, ¶ 66.09[1] (2d ed. 1985).

[14] The Bankruptcy Act of 1867, ch. 176, 14 Stat. 517 (repealed by Act of June 7, 1878, ch. 160, 20 Stat. 99 *et seq.*), did not provide viable mechanisms for forcing creditors to accept consolidation or composition of debts, and the United States had no general bankruptcy code from 1878 to 1898. See 1 *Collier on Bankruptcy* § 0.05 (14th ed. 1978). Thus, receiverships were originally instituted with full knowledge that a partial or complete foreclosure was a likely prospect. See 3 R. Clark, *The Law and Practice of Receivers* §§ 855-857 (3d ed. 1959). However, the railroads eventually became skilled at using the equity receivership for reorganization purposes, often to the detriment of creditors and the public. See *Securities and Exchange Commission Report on the Study and Investigation, Personnel and Functions of Protective and Reorganization Committees: Strategy and Techniques of Protective and Reorganization Committees*, Pt. 1 (May 10, 1937) (*reprinted in part in* H.R. Rep. 95-595, 95th Cong., 1st Sess. 242-244 (1977)). The resulting abuses eventually led to the adoption of provisions in the 1930's for reorganization in bankruptcy. See H.R. Rep. 95-595, *supra*, at 242, 244.

that the provision without question was intended to reach, such as the abandonment of state-regulated rail service,[15] was likely to occur in liquidation. Thus, Section 959(b)'s legislative origins fully support its application to actions taken by a trustee in liquidating a bankruptcy estate.

Setting aside lexicon and legislative history, the underlying purposes of Section 959(b) require its application to liquidation as well as to the operation of ongoing businesses. The section is intended to advance federalism interests by limiting the power of federal court appointees to avoid state law. There are no sound reasons for requiring federal trustees to comply with state laws when operating a business, but permitting them to disregard those same laws when liquidating the enterprise. If a trustee seeks, for example, to sell adulterated food, controlled substances, or dangerous products to the general public, pursuant to his powers under 11 U.S.C. 363, it should make little difference whether he is operating the debtor's business or liquidating its assets. The effective result of freeing the trustee from state law is the same in either case—intrusion on state legislative and executive mechanisms by a federal court appointee who is unaccountable to the public and perhaps insensitive to state and local concerns.[16]

[15] See, *e.g.*, *Palmer* v. *Massachusetts*, 308 U.S. 79 (1939); *In re Chicago Rapid Transit Co.*, 129 F.2d 1, 6 (7th Cir.), cert. denied, 317 U.S. 683 (1942); *Crawford* v. *Duluth St. Ry.*, 60 F.2d 212, 215 (7th Cir. 1932).

[16] Petitioner Midlantic suggests (84-801 Br. 24) that the dictum in *Missouri* v. *United States Bankruptcy Court*, 647 F.2d 768, 778 n.18 (8th Cir. 1981), cert. denied, 454 U.S. 1162 (1982), expressing some "doubt" that a bankruptcy trustee must obtain a state license to sell grain when liquidating the assets of a grain warehouse, demonstrates that Section 959(b) is inapplicable to liquidation proceedings. The court's tentative dictum is hardly persuasive. Even if correct (which *we doubt*), it speaks only to the procedural aspects of sale, which would seem to be more susceptible to federal pre-

Section 959(b) is limited, of course, to "valid" state law. It presumably would not operate where the Bankruptcy Code unequivocally preempts the state law or where the state takes action that specifically discriminates against the trustee.[17] But these are narrow exceptions. As a general matter, Section 959(b) demonstrates that a bankruptcy trustee is subject to state police powers in administering the estate, except where the Bankruptcy Code expressly or by necessary implication provides otherwise.

B. Section 554 Of The Bankruptcy Code, Which Authorizes The Trustee To Abandon Financially Burdensome Property, Does Not Preempt Generally Applicable Laws Safeguarding Public Health And Safety

As the preceding section explains, a bankruptcy trustee must generally exercise his powers in accordance with state law. This proposition holds true when the trustee exercises his specific power of abandonment under Section 554 of the Bankruptcy Code, 11 U.S.C. 554. Section 554 codifies a judge-made rule of abandonment and thereby adopts the longstanding judicial corollary that a trustee's abandonment power is subject to general police power regulations. The legislative history of the 1978 Bankruptcy Reform Act confirms that Section 554, far from preempting state law, actually embraces its application.

The 1978 Bankruptcy Reform Act originated in the recommendations presented to Congress by the Commis-

emption. Indeed, it appears that the Eighth Circuit would agree that the trustee could not sell the grain if state law absolutely forbade its sale on public health grounds rather than simply regulated who sold it. See 647 F.2d at 776 (noting the Bankruptcy Code's deference to state health and safety laws).

[17] For example, the Bankruptcy Code, rather than state law, governs distribution of the estate. *American Surety Co.* v. *Sampsell*, 327 U.S. 269, 272 (1946). The mere fact that state law requires financial expenditures does not, of course, alter distribution priorities. See *Gillis* v. *California*, 293 U.S. 62, 66 (1934).

sion on the Bankruptcy Laws of the United States. See Pub. L. No. 91-354, 84 Stat. 468-469. The Commission's final report included a proposed bill that served as a blueprint for many portions of the 1978 Act. Section 4-611 of that bill expressly recognized the trustee's power to abandon property of the estate "if it is burdensome or has no net realizable value." *Report of the Commission on the Bankruptcy Laws of the United States*, H.R. Doc. 93-137 93d Cong., 1st Sess., Pt. 2, at 181 (1973). Citing 4A *Collier on Bankruptcy* ¶ 70.42[3] (1967), the accompanying Commission Note stated that "[t]he concept of abandonment is well recognized in the case law," H.R. Doc. 93-137, *supra*, Pt. 2, at 181. Although the 1898 Bankruptcy Act contained no abandonment provision, the Commission Note indicated that its proposal was adopted from Bankruptcy Rule 608, promulgated under that Act. H.R. Doc. 93-137, *supra*, Pt. 2, at 181. Rule 608, in turn, contained similar language, and its accompanying Advisory Note expressly stated that the Rule "codifie[d] the preferred practice developed under case law." Bankruptcy Rule 608 advisory committee note, 11 U.S.C. App., at 227.

Congress, apparently relying on the Commission's recommendations, fashioned Section 554 in close conformity to the Commission's proposal. Additionally, Congress provided no further elaboration on the section's scope. Thus, Congress, like the Commission and the Bankruptcy Rules Advisory Committee, must have intended to codify the traditional judge-made abandonment rules. Notably, Congress offered no definition of the term "abandon," a bankruptcy term of art that could only be understood by reference to past bankruptcy practices. It follows that the "plain meaning" of Section 554 is, by necessity, the meaning generated by those practices. Indeed, Congress's failure to elaborate on the reach of Section 554 "is most eloquent, for such reticence while contemplating an important and controversial change in existing law is unlikely." *Edmonds* v. *Compagnie Generale Transatlantique*, 443 U.S. 256, 266-267 (1979) (footnote omitted).

Congress is, of course, presumed to have codified the judge-made law existing at the time of its consideration and enactment of Section 554. See *Merrill Lynch, Pierce, Fenner & Smith, Inc.* v. *Curran*, 456 U.S. 353, 379-382 (1982); *Lorillard* v. *Pons*, 434 U.S. 575, 580-581 (1978). At the time that Congress considered and enacted Section 554, the trustee's responsibility to exercise his abandonment powers consistent with federal and state police powers was well established. As a leading bankruptcy treatise noted (4A *Collier on Bankruptcy* ¶ 70.42[2] (14th ed. 1978) (emphasis added; footnotes omitted)):

> The trustee (and in a proper case, the receiver before him) may abandon any property which is either worthless, or overburdened, or for any other reason certain not to yield any benefit to the general estate. *Recent cases illustrate, however, that the trustee in the exercise of the power to abandon is subject to the application of general regulations of a police nature.*

Accord, 2 H. Remington, *A Treatise on the Bankruptcy Law of the United States* § 1142, at 623 (1956).

The Collier treatise specifically cited two cases, *Ottenheimer* v. *Whitaker*, 198 F.2d 289 (4th Cir.), aff'g *In re Eastern Transp. Co.*, 102 F. Supp. 913 (D. Md. 1952), and *In re Chicago Rapid Transit Co.*, 129 F.2d 1 (7th Cir.), cert. denied, 317 U.S. 683 (1942). In *Ottenheimer*, the court of appeals concluded that a bankruptcy trustee, in liquidating the estate of a barge company, could not abandon several dilapidated barges moored in Baltimore Harbor, because the abandonment would have resulted in a navigational obstruction in violation of federal law. The court stated (198 F.2d at 290):

> The judge-made [abandonment] rule must give way when it comes into conflict with a statute enacted in order to ensure the safety of navigation; for we are not dealing with a burden imposed upon the bankrupt or his property by contract, but a duty and a burden imposed upon an owner of vessels by an Act of Congress in the public interest.

The court in *In re Chicapo Rapid Transit* reached a similar result. In that case, a reorganization trustee sought to abandon the debtor transit company's lease of a branch railway line, notwithstanding local law that required continued operation. The court recognized that a bankruptcy court could "not order the utility to abandon a public service, without consent of the state" (129 F.2d at 5), but that it could "cancel a burdensome lease" (*ibid.*). The court, noting that the lessor and lessee both were obligated under a local ordinance to operate the branch line (129 F.2d at 7-8), reconciled the two competing considerations by permitting the trustee to abandon the unexpired lease, but requiring him to continue operations for the account of the lessor. *Id.* at 5-6. Thus, while the court did not forbid the trustee's abandonment of property (or perhaps, more accurately, his rejection of an unexpired lease), it conditioned the trustee's actions to ensure compliance with state law. Notably, the court relied, in part, on the predecessor of 28 U.S.C. 959(b)—28 U.S.C. 124—in concluding that the trustee was bound by state law. 129 F.2d at 6.

Ottenheimer and *Chicago Rapid Transit* demonstrate that a trustee's abandonment power, prior to the 1978 Bankruptcy Reform Act, was limited by federal and state police powers.[18] These mutually consistent cases were well-established and, indeed, recounted in the leading bank-

[18] A third case, *In re Lewis Jones, Inc.*, 1 Bankr. Ct. Dec. (CRR) 277 (Bankr. E.D. Pa. 1974), offers still further support for this proposition. *Lewis Jones* involved the bankruptcy liquidation of three public utilities that supplied steam heat to city residents. The trustees sought to abandon underground steam lines; however, several governmental entities objected to the trustees' plan because it did not provide for sealing the abandoned lines. The governmental bodies cited various health and safety hazards that would result. The bankruptcy court noted that *Ottenheimer* required compliance with local laws but found none applicable. It nevertheless required the trustees to seal the steam lines, citing the court's equitable power to "safeguard the public interest." 1 Bankr. Ct. Dec. at 280.

ruptcy treatises when Congress codified the trustee's abandonment power. They therefore reflect congressional understanding of the traditional reach of abandonment in bankruptcy and control the interpretation of Section 554.[19]

Petitioners nonetheless contend (*e.g.*, 84-801 Br. 16-26) that Section 554 creates an absolute right to abandon property, regardless of contrary federal or state law. This contention is fatally undermined by the general rule that the trustee must comply with non-bankruptcy law, by the express limitation contained in 28 U.S.C. 959(b), and by the legislative history of Section 554, which clearly indicates that Congress adopted the recognized judicial limitations on the trustee's abandonment power.[20] Indeed, petitioners actually urge a radical and unwarranted *expansion* of the trustee's traditional abandonment power.

Historically, the trustee's abandonment power has been directed solely to property suffering from contractual, rather than regulatory, encumbrances.[21] Thus, abandonment principles were originally developed to protect the trustee from personal liability for the contractual commitments of the debtor.[22] Under present bankruptcy law, however, the trustee is merely a representative of the estate (11 U.S.C. 323(a)), and he is not subject to personal liability for the estate's obligations. In the modern context, therefore, abandonment is simply a method for

[19] The only authority that is even arguably contrary to *Ottenheimer* and *Chicago Rapid Transit* is *In re Adelphi Hospital Corp.*, 579 F.2d 726 (2d Cir. 1978) (per curiam). *Adelphi Hospital* involved the bankruptcy liquidation of a privately-owned hospital. The trustee sought to abandon patient records. The state objected, interposing state regulations that required the "governing authority" of a discontinued hospital to retain hospital records for six years. The court of appeals concluded that the trustee was not a "governing authority" and therefore was not bound by the regulations. 579 F.2d at 728. The court also suggested that the trustee's abandonment power was relatively broad, citing, ironically, *In re Chicago Rapid Transit Co. Adelphi Hospital*, 579 F.2d at 729. Although this per curiam dicta might be read to depart from *Ottenheimer*, it does not create an irreconcilable conflict that beclouds congressional intent. Compare *NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 10. In all events, the case was decided just a few months before enactment of Section 554 and therefore cannot reasonably be considered within congressional contemplation. See *City of Milwaukee* v. *Illinois*, 451 U.S. 304, 327 n.19 (1981).

[20] The Trustee casually dismisses *Ottenheimer* in a footnote (84-805 Br. 24 n.7) and does not even acknowledge *Chicago Rapid Transit*. Petitioner Midlantic, meanwhile, suggests that *Ottenheimer* would have been decided differently if Section 554 had then been in existence (84-801 Br. 20). Thus, petitioners fail to come to grips with the central weakness of their argument: Congress, in enacting Section 554, did not write upon a *tabula rasa*; instead, it codified the judicially-developed rule of abandonment, including the established corollary that the trustee must exercise his abandonment power in conformity with federal and state law.

[21] *E.g.*, *McHenry* v. *La Societe Francaise D'Epargnes*, 95 U.S. 58, 60 (1877). Although the early American cases adopting abandonment principles spoke broadly of a trustee's power to decline "property of an onerous or unprofitable character," *e.g.*, *First National Bank* v. *Lasater*, 196 U.S. 115, 118 (1905), the cases all seemingly contemplated property burdened by liens, mortgages, or contractual commitments. See *Dushane* v. *Beall*, 161 U.S. 513 (1896); *Sparhawk* v. *Yerkes*, 142 U.S. 1 (1891); *American File Co.* v. *Garrett*, 110 U.S. 288 (1884); *Glenny* v. *Langdon*, 98 U.S. 20 (1878); *Smith* v. *Gordon*, 22 Fed. Cas. 554 (D. Me. 1843) (No. 13,052). See also Note, *Abandonment of Assets by a Trustee in Bankruptcy*, 53 Colum. L. Rev. 415, 416-417 (1953).

[22] American courts adopted their judge-made rule of abandonment from early English bankruptcy statutes. See 4A *Collier on Bankruptcy* ¶ 70.42[1], at 501 (14th ed. 1978). Under English law, the trustee needed a means of avoiding any contractual liability that might accompany the vesting of title. As a contemporary commentator explained:

> [I]nasmuch as the leasehold estates of the bankrupt vested in his trustee, the Legislature was obliged to provide a means for the trustee to get rid of his liability in respect to those leasehold estates. Sect. 23 was passed for this purpose * * *.

Ringwood, *The Disclaimer of Onerous Property in Bankruptcy*, 82 The Law Times 142 (London, Dec. 25, 1886). See also *A Bankrupt's Onerous Property*, 53 The Justice of the Peace 339 (London, June 1, 1889).

avoiding transaction costs when administering the estate. It permits the trustee to exclude from the estate "property not expected to sell for a price sufficiently in excess of the mortgage or judgment liens to offset the interest and costs of administration." Note, *Abandonment of Assets by a Trustee in Bankruptcy*, 53 Colum. L. Rev. 415, 416 (1953). But there is no support for the notion that Section 554, enacted simply to permit efficient administration of the bankruptcy estate, was ever intended to override traditional governmental authority to protect public health and safety. Clearly, no such intent should be attributed to Congress absent affirmative evidence that it desired such a radical result. See *Swarts* v. *Hammer*, 194 U.S. 441, 444 (1904); *Palmer* v. *Massachusetts*, 308 U.S. 79, 89 (1939).

This Court's recent decision in *Ohio* v. *Kovacs*, No. 83-1020 (Jan. 9, 1985), does not compel a different conclusion. In dictum, the Court observed that a trustee, as a general matter, can abandon a hazardous waste site just as he might abandon any other property. *Kovacs*, slip op. 10 n.12. We might agree that there is nothing unique about a waste site that, in the abstract, distinguishes it from other types of property and excepts it from the trustee's abandonment power. But the same can be said of dilapidated barges or, for that matter, a case of dynamite. A far different question is implicated when the dilapidated barges are moored at the mouth of Baltimore Harbor or, more hypothetically, the case of dynamite sits on a furnace in the basement of a schoolhouse. The question in this case, which was not addressed in *Kovacs*, is whether the trustee may abandon property within his custodial care when the act of abandonment itself would create or contribute to a public health and safety threat. Nothing in *Kovacs* suggests that the federal and state governments, in the exercise of their respective police powers, are powerless to prevent the trustee from abandoning property when, under the circumstances, abandonment itself significantly increases the risk of public harm.

C. New Jersey And New York Public Nuisance Law Limits The Trustee's Authority To Abandon Hazardous Wastes And Related Property

Given that the Trustee's authority to abandon burdensome property is subject to state police powers, the only remaining question is whether New York or New Jersey law actually limits the Trustee's authority in the circumstances presented by this case. The court of appeals observed that state environmental statutes could impose relevant limitations (Pet. App. 4a, 6a, 38a). However, the application of these laws is far from clear, and we leave it to respondents to clarify the applicability of their own laws. For our part, we believe that state public nuisance law provides the most reasonable and workable restraint on the Trustee's abandonment power in this case (see note 35, *infra*).[23] In either event, the court of appeals' judgments must be affirmed.[24]

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[23] State public nuisance law, developed largely through the common law process, is entitled to no less respect than state statutory law. See, *e.g.*, *Erie R.R.* v. *Tompkins*, 304 U.S. 64, 78 (1938) ("[W]hether the law of the State shall be declared by its Legislature in a statute or by its highest court in a decision is not a matter of federal concern."); cf. *National Farmers Union Ins. Cos.* v. *Crow Tribe of Indians*, No. 84-320 (June 3, 1985), slip op. 4-5. Indeed, the flexibility inherent in nuisance law, reflecting its equitable origins, make its application particularly appropriate in bankruptcy proceedings. See notes 33-35, *infra*. See also *In re Chicago, R.I. & P. R.R.*, 756 F.2d 517 (7th Cir. 1985) (considering nuisance principles in bankruptcy); *In re Lewis Jones, Inc.*, 1 Bankr. Ct. Dec. (CRR) 277, 280 (Bankr. E.D. Pa. 1974) (discussed at note 18, *supra*).

[24] We note that the sole issue decided by the court of appeals and now before this Court is whether Section 554 gives the Trustee an absolute right to abandon the property at issue, regardless of otherwise applicable law (see Pet. App. 3a, 36a-37a). Both the district court and the bankruptcy court concluded that the Trustee's power was absolute (see *id.* at 57a, 72a-73a), and both New York and NJDEP challenged that specific conclusion on appeal. The court of appeals reversed, holding that Congress did not intend "that the trustee's abandonment power be unrestricted by public

Each state, as a core element of its sovereignty, has indisputably broad authority to prohibit and abate, as a public nuisance, conduct and activity inimical to the public at large. *E.g.*, *Lawton* v. *Steele*, 152 U.S. 133, 136 (1894); see generally *Prosser & Keeton on Torts*, 649-652 (W. Keeton 5th ed. 1984); Restatement (Second) of Torts § 821B (1979).[25] The creation and maintenance of hazardous wastes in a manner that threatens public health and safety unquestionably presents a public nuisance that is subject to abatement.[26] The Trustee's abandonment of hazardous wastes and related property, at least when the abandonment itself creates or aggravates a public health and safety threat, is likewise subject to reasonable restraints.

State law recognizes that abandonment of even the most innocuous property, without prudent precautions, can threaten public health or welfare and create an enjoinable nuisance.[27] The irresponsible abandonment of inherently hazardous wastes poses particularly alarming health and safety concerns. Hazardous wastes, by their very nature, present risks of explosion, fire, contamination of water supplies, destruction of natural resources, and injury, genetic damage, or death through personal contact. When they are abandoned without basic custodial precautions, such as containment measures and provisions for site security, these risks become imminent and their realization inevitable. A state is entitled to invoke its police powers in response.

Contrary to petitioners' suggestions, a bankruptcy trustee cannot claim a special immunity from state demands for pre-abandonment protective measures. A trustee does have fiduciary obligations to creditors (84-805 Br. 26), but he cannot blindly pursue creditors' interests, oblivious to public health and safety threats left in his wake. See, *e.g.*, Restatement (Second) of Trusts §§ 62, 166 (1959) (a trustee is under no obligation to undertake acts that are against public policy or illegal). Although it is true that abandonment in bankruptcy vests title to the property in the debtor corporation rather than the public at large (84-801 Br. 17; 84-805 Br. 36-

health and safety regulations" (*id.* at 9a; see also *id.* at 39a), and remanded for further proceedings. In the course of its decision, the court did need to ascertain that some source of state law would impose potential limitations on the Trustee's powers and that this case therefore presented a justiciable controversy. However, the court of appeals' holding does not depend on its view of the applicable state law; the judgments can be affirmed regardless of the source of state law that limits the Trustee's abandonment powers. See *Black* v. *Cutter Laboratories*, 351 U.S. 292, 297 (1956) ("This Court * * * reviews judgments, not statements in opinions.").

[25] See also, *e.g.*, *State ex rel. Board of Health* v. *Sommers Rendering Co.*, 66 N.J. Super. 334, 338, 169 A.2d 165, 167 (1961) (rendering plant odors); *New York Trap Rock Corp.* v. *Town of Clarkstown*, 299 N.Y. 77, 80, 85 N.E.2d 873, 875 (1949) (quarry operations). See also N.J. Stat. Ann. §§ 2C:17-2, 2C:33-12 (West 1982); N.Y. Penal Law § 240.45 (McKinney 1982) (criminal provisions for knowingly creating or maintaining a public nuisance). But see *Murphy* v. *United States*, 272 U.S. 630, 632 (1926) (government "may provide for the abatement of a nuisance whether or not the owners of it have been guilty of a crime").

[26] *E.g.*, *State* v. *Ventron Corp.*, 94 N.J. 473, 468 A.2d 150, 160 (1983); *State* v. *Monarch Chemicals, Inc.*, 90 A.D.2d 907, 908, 456 N.Y.S.2d 867, 869 (1982).

[27] The issue arises frequently with respect to abandoned buildings. *E.g.*, *Beauchamp* v. *New York City Housing Authority*, 12 N.Y.2d 400, 406-407 (1963); *Ozone Holding Corp.* v. *City of New York*, 79 Misc.2d 744, 748, 361 N.Y.S.2d 558, 563 (1974). However, the abandonment of virtually any property that threatens public harm can result in a nuisance. See, *e.g.*, *Cady* v. *Dombrowski*, 413 U.S. 433, 447 (1973) (abandoned vehicle) (dicta); *Price* v. *City of Junction*, 711 F.2d 582, 585-587 & n.2 (5th Cir. 1983) (abandoned vehicle); *Skinner* v. *Coy*, 13 Cal.2d 407, 417-418, 90 P.2d 296, 300-301 (1939) (abandoned diseased plants); *Decker* v. *Jones*, 194 Kan. 146, 147, 398 P.2d 325, 326 (1965) (abandoned oil and gas drilling equipment); *Touro Synagogue* v. *Goodwill Industries, Inc.*, 233 La. 26, 30, 34, 96 So.2d 29, 30, 32 (1957) (abandoned cemetery); *Massachusetts Society for the Prevention of Cruelty to Animals* v. *Commissioner of Public Health*, 339 Mass. 216, 225-226, 158 N.E.2d 487, 493-494 (1959) (abandoned animals); *Commonwealth* v. *Barnes & Tucker Co.*, 472 Pa. 115, 126, 371 A.2d 461, 466-467, appeal dismissed, 434 U.S. 807 (1977) (abandoned mine).

37), that consequence does not give rise to a meaningful distinction. The filing of the bankruptcy petition divested the debtor of its assets and placed them within the *trustee's* exclusive control. The debtor is destined to exist indefinitely as an empty husk and eventually dissolve, leaving no one accountable for the property. See *Ohio* v. *Kovacs*, No. 83-1020 (Jan. 9, 1985) (O'Connor, J., concurring), slip op. 2. Thus, abandonment to the assetless and evanescent corporate debtor has the very same effect as abandonment to the public at large.[28] Furthermore, the fact that the trustee does not own the property (84-801 Br. 17) cannot permit him to ignore the dangers created by *his* decision to abandon it. The trustee is the custodian of the property and is charged with its care. 11 U.S.C. 704(2). He is not entitled to endanger the public simply because he acts on behalf of the estate.[29] Likewise, the preexisting dangerous propensities of the property do not give him license to increase or

[28] Petitioner Midlantic's argument (84-801 Br. 17) that *Brown* v. *O'Keefe*, 300 U.S. 598 (1937), absolves the trustee of all responsibility for abandonment is an attempt to elevate the trustee, by his bootstraps, to a position above the law. *Brown's* holding that abandonment under the 1898 Bankruptcy Act relates back to the filing of the bankruptcy petition is simply not relevant to whether abandonment is proper in the first instance.

[29] *Reading Co.* v. *Brown*, 391 U.S. 471 (1968), amply demonstrates this point. The trustee's post-petition negligence in administering an estate led to a fire that damaged adjoining buildings. This Court recognized the trustee's duty to prevent the occurrence (*id.* at 477), and concluded that the resulting tort claim was an administrative expense of the estate (*id.* at 482). Just as a trustee owes a duty, on behalf of the estate, of reasonable care to adjoining landowners, he owes a duty to the general public to avoid creating or aggravating a threat of public harm. See also, *e.g.*, *In re Chicago, R.I. & P. R.R.*, 756 F.2d 517, 521-522 (7th Cir. 1985) (suggesting that a trustee may not abandon railroad crossings if the abandonment would create imminent danger); *In re Vermont Real Estate Investment Trust*, 25 Bankr. 804, 806 (Bankr. D. Vt. 1982) (recognizing that a debtor-in-possession or a trustee owed a duty to the public to raze a dangerous building).

aggravate the public threat through abandonment.[30] He has no right to worsen an already dangerous situation. Accord, Hennigan, *Accommodating Regulatory Enforcement and Bankruptcy Protection*, 59 Am. Bankr. L.J. 1, 54 n. 257 (1985).[31]

In sum, the trustee is not immune from a state's exercise of its traditional powers, under public nuisance law, to protect its citizen's health and safety.[32] Nonetheless,

[30] See, *e.g.*, *State* v. *Schenectady Chemicals, Inc.*, 117 Misc.2d 960, 966, 459 N.Y.S.2d 971, 976-977 (1983), aff'd, 103 A.D.2d 33, 479 N.Y.S.2d 1010 (1984). The Trustee claims that abandonment did not cause any threat to the public (84-805 Br. 33). However, the realities of the Trustee's actions belie that assertion. By abandoning the property, the Trustee severed the hazardous wastes from his custodial care and from what financial resources were available to protect the public from imminent harm. For example, upon abandonment, the Trustee's security measures—which prevented public entry, vandalism, and arson—were terminated and all maintenance and remedial measures, initiated by Quanta, came to a halt. Thus, abandonment seriously aggravated the dangers first created by Quanta.

[31] Likewise, it is no answer to suggest that the public assume all responsibility for the consequences of abandonment (84-801 Br. 25-26; 84-805 Br. 37-38). The principles of public nuisance law are expressly intended to assure, to the extent possible, that responsible parties *prevent* threats to the public. A bankruptcy trustee has no greater right than any other party to foist burdens on the public at large. Compare *In re Vermont Real Estate Trust*, 25 Bankr. 804 (Bankr. D. Vt. 1982), with *Paterson* v. *Fargo Realty Inc.*, 174 N.J. Super. 178, 415 A.2d 1210 (1980).

[32] The application of federal hazardous waste statutes is not at issue in this case. We note, however, that those laws, apart from providing other conceivably relevant restrictions, impose limitations analogous to state nuisance law on activities involving hazardous wastes. The Resource Conservation and Recovery Act of 1976 (RCRA), 42 U.S.C. 6901 *et seq.*, in addition to providing a comprehensive regulatory scheme, empowers the United States to seek judicial or administrative restraint of activities involving hazardous wastes that "may present an imminent and substantial endangerment to health or the environment." 42 U.S.C. 6973. The United States may act against "any person contributing to [the] handling,

nuisance law, which relies on principles of reasonableness,[33] does not absolutely proscribe abandonment. Instead, it requires that the trustee, prior to abandonment, take steps that are reasonable in light of the circumstances to protect the public from harm. In determining what steps are reasonable, the magnitude of the public threat is, of course, highly relevant. But of like relevance are the resources of the estate. A trustee cannot be asked to do more than available funds permit; the pre-conditions for abandonment cannot be so costly that they exceed the value of the estate.[34] A court, in determining whether,

storage, treatment, transportation or disposal" of hazardous wastes. *Ibid.* See also S. Rep. 98-284, 98th Cong., 1st Sess. 58 (1983) (1984 RCRA Amendments). The United States possesses similar authority under CERCLA to secure such relief as may be necessary to avert an "imminent and substantial endangerment to the public health or welfare or the environment because of an actual or threatened release of a hazardous substance." 42 U.S.C. 9606. These particular provisions of RCRA and CERCLA represent a legislative application of public nuisance concepts to protect the public from the dangers of hazardous wastes. See *United States* v. *Waste Industries, Inc.*, 734 F.2d 159, 167 (4th Cir. 1984). The United States may invoke these provisions in a bankruptcy proceeding to prevent a trustee from abandoning hazardous wastes and related property if abandonment would contribute to an imminent and substantial endangerment to health and the environment.

[33] *E.g., Beauchamp* v. *New York City Housing Authority*, 12 N.Y.2d 400, 407 (1963); *State* v. *Waterloo Stock Car Raceway, Inc.*, 96 Misc.2d 350, 409 N.Y.S.2d 40, 45 (Sup. Ct. 1978). See generally Restatement (Second) of Torts § 821B comment e (1979).

[34] Expenses resulting from the pre-abandonment abatement of imminent dangers must generally be paid from estate funds. See, *e.g., Reading Co.* v. *Brown*, 391 U.S. 471, 477 n.7 (1968). Thus, a court cannot reasonably require a trustee to undertake abatement actions that cost more than the estate can pay. The degree of abatement must therefore depend on both the dangers presented by abandonment *and* the available resources of the estate. We note, in this regard, that there is no merit to petitioners' claims that they will suffer ruinous liability absent an absolute right of abandonment (84-805 Br. 18-19; 84-801 Br. 11-12). Absent highly unusual circumstances, such as a trustee's operation of the hazardous waste site or the intentional misconduct of a trustee, the estate alone is responsible for the abatement costs. Likewise, secured claims will be compromised only to the extent that the abatement costs are administrative expenses necessary to preserve or dispose of the security. See 11 U.S.C. 506; see also pages 28-29, *infra*.

and under what conditions, abandonment is permissible, must balance competing bankruptcy and nonbankruptcy considerations. There is, of course, nothing novel in this process; bankruptcy law frequently requires the exercise of such essentially equitable judgments. Indeed, this Court, in other contexts, has recognized that "the policies of flexibility and equity" are inherent in the Bankruptcy Code. *E.g., NLRB* v. *Bildisco & Bildisco*, No. 82-818 (Feb. 22, 1984), slip op. 10.[35]

In our submission, the present cases must be remanded for a precise application of state law. What is clear is that the district and bankruptcy courts erred in permitting abandonment of hazardous wastes and related property without considering *any* precautions to protect the public health and safety. On remand, the lower courts can determine what actions the Trustee should have taken and how those who acted in his stead should be recompensed.[36]

[35] In this respect, we believe that grounding the trustee's responsibilities in the specific and somewhat less flexible requirements of state environmental statutes could conceivably thwart the administration of the bankruptcy estate and therefore raise bona fide, albeit case-specific, preemption concerns. By contrast, the inherent flexibility of nuisance principles, applied in the bankruptcy proceeding to the specific facts at hand, avoids this potential problem. Of course, state statutes may be highly relevant, as an indication of the public's interest, in the nuisance analysis.

[36] The question of appropriate pre-abandonment measures cannot be determined on the present record. However, EPA's "immediate removal" activities at the Edgewater site (see note 3, *supra*) are likely examples of reasonable pre-abandonment requirements. These activities include security fencing, drainage and diking repairs, and removal of explosive agents and hazardous materials from structurally infirm tanks. See EPA Region II Action Memorandum (Jan. 25, 1985) (lodged with the Court).

D. State Law Limitations On The Trustee's Abandonment Power Do Not Threaten A Taking Of Creditors' Property Rights

Citing *United States* v. *Security Industrial Bank*, 459 U.S. 70 (1982), petitioners argue that Section 554 must be read to permit unfettered abandonment so as to avoid any possible Fifth Amendment taking of creditors' interests. This argument is plainly meritless; the present case does not raise any constitutional threats to creditors' property rights.

The court of appeals addressed only one issue—whether the Trustee has an unconditional right to abandon burdensome property. It determined that he did not, and remanded to the lower courts to determine what action he should take and how the associated expenses should be funded. The court of appeals left fully intact the Bankruptcy Code's liquidation distribution provisions. Holders of secured claims, such as petitioner Midlantic, remain entitled to their security, 11 U.S.C. 725, or proceeds from its sale, 11 U.S.C. 363, less applicable administrative expenses, 11 U.S.C. 506(c). Holders of unsecured claims remain subordinated to priority claims, which again include administrative expenses, 11 U.S.C. 726. The court did not alter the status of creditors' claims; thus, it is difficult to discern any constitutional threat to creditors' interests.

As the court of appeals recognized (but did not decide), cleanup expenditures might constitute an administrative expense. Indeed, we believe that lawful pre-abandonment expenditures should be so treated. See, *e.g.*, *In re T. P. Long Chemical, Inc.*, 45 Bankr. 278 (Bankr. N.D. Ohio 1985).[37] But any argument that ad-

ministrative expense treatment of cleanup claims would work an unconstitutional taking is unpersuasive. The potential administrative expense claims do not threaten secured creditors, save those who hold an interest in the hazardous waste site or the wastes themselves and who, as a result, might be subject to a Section 506(c) assessment for costs incurred in preserving their security. See 11 U.S.C. 506(c). In all events, the Quanta waste site and the wastes, prior to cleanup, had negative value and, hence, there was nothing to be taken. Likewise, a post-cleanup Section 506(c) claim presumably would be limited to the value added to the property by the cleanup—hardly a taking in any sense of the word. If petitioners are suggesting that general unsecured creditors face a taking because the administrative expenses subordinate unsecured claims, a traditional takings analysis, as set forth in the court of appeals' opinion (Pet. App. 23a n.11), provides the appropriate response. Even if an unsecured claim in bankruptcy constituted "property" within the meaning of the Fifth Amendment, it would remain subject to federal and state police power. See cases cited at note 5, *supra*. If the federal and state governments can legitimately impose cleanup costs on the corporation prior to bankruptcy, there is no reason why any unsecured creditor who undertook the risk of non-payment can complain about the resulting diminishment of the debtor's estate.

[37] Compare *Southern Ry.* v. *Johnson Bronze Co.*, 758 F.2d 137 (3d Cir. 1985). In that case, a debtor, prior to bankruptcy, left hazardous wastes on the property of an adjacent landowner and on property that the debtor leased. The adjacent landowner and the post-petition assignee of the lease claimed that they were entitled to an administrative priority for their cleanup costs arising from the debtor's pre-petition activities. The court concluded that the landowner had an unsecured claim and that the assignee, assuming the lease with notice of the wastes, had no claim at all. These claims are quite different from those that are available in the Quanta bankruptcy. New York and NJDEP, as governmental entities, have legitimate administrative expense claims for post-petition activities that state nuisance law *obligated* the Trustee to undertake prior to abandoning hazardous wastes and related property.

CONCLUSION

The judgments of the court of appeals should be affirmed.

Respectfully submitted.

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